KPMG
cutting through complexity

Financing family business growth:

Bringing family businesses and investors together

kpmgfamilybusiness.com

WomenCorporateDirectors
globally accelerating best practices in corporate governance

Contents

Introduction

In September 2014, KPMG released its first Global Family Business Survey *Family matters: Financing family business growth through individual investors*. The report examined the sources of funding available for family businesses and explored the synergies between family businesses and high-net-worth individuals (HNWIs) as suitable investment partners. Drilling down into the relationship between the two groups, the report outlined the opportunities and identified how HNWIs and family businesses can make excellent business partners, as HNWIs are able to bridge the existing financing gap resulting in a lasting and productive partnership.

The Global Survey was backed by a common understanding that despite the fact, that like any other company, family businesses need financing to execute their growth and development plans. Their unique nature and a number of characteristics impose limits on finding suitable funding. These attributes include a strong desire among family owners to retain control of the business, an emphasis on managing the company with longevity in mind and a desire for the intricacies of the family business to remain confidential. While some family businesses may look to traditional sources of financing, such as private equity (PE) firms or corporate strategic partners, these sources are not able to meet many of the desired requirements that family businesses seek in a funding partner. The strong desire of family businesses to retain majority ownership creates an opportunity for HNWIs to be better suited investment partners to family businesses.

The personal interviews conducted by KPMG with their family business clients revealed that an underutilized route for investments is to partner with HNWIs. These investors are more willing to accept minority stakes, without ambitions to secure full control of the business or a full sale in the future. They are also likely to

have experience relevant to the family businesses they are investing in and may have a similar attitude in terms of investment time frames and risk.

In order to explore how family businesses and HNWIs can work together, Mergermarket, on behalf of KPMG International, surveyed 125 family businesses and 125 HNWIs from 29 countries (covering a total of 82.4 percent of global GDP). They asked family businesses about the funding investments they were seeking, their choice for investors, and their previous experience of receiving investment from HNWIs and other family businesses. HNWIs were surveyed about their investment strategies and how their preferences may align with family businesses.

The Global Survey revealed that despite challenges on both sides, both parties have an appetite for investment and could prove to make excellent partners. The report also identified steps which can be taken to improve the efficiency of this underutilized source of capital.

Backed by these findings, WomenCorporateDirectors (WCD), together with KPMG, decided to take a closer look at how this type of funding partnership is perceived and represented among WCD members, and whether there is anything unique about their responses.

Using the same questions as the Global Survey, we collected responses from over 40 family businesses and HNWIs from the WCD network worldwide. Christine Blondel, Adjunct Professor of Family Business at INSEAD and Senior Advisor to KPMG on Family Business Intelligence, has further spoken with several of our members to collect their views on this funding partnership and on possible routes for family businesses and HNWIs to work together.

The WCD Survey reveals that despite some obvious similarities between the experiences and views of WCD members and the global business community we surveyed, there are still a number of significant differences. Moving forward, it may be interesting to explore what lies behind these differences, what WCD members can teach other family businesses and HNWIs, and what they can learn from them.

Financing needs of family businesses

Financing needs of family businesses

Highlights

1

The majority of WCD family businesses have a **significant amount of family member involvement – with 90 percent of businesses surveyed** owned by family members with a majority stake.

2

Family businesses are quite amenable to offering equity to the right type of investor. Eighty-four percent of respondents reported that the **biggest fear is loss of independence**.

3

Family **values and ethics and other intangible assets play a vital role** for family firms as it relates to the way they do business, including their choice of investment partners.

4

Family business owners realize the **importance of additional knowledge and expertise** and almost half (42 percent) rate it as the most valued benefit an external investor can bring.

Family businesses stay close to family

Having built and developed the company through multiple generations, families wish to maintain strong links through majority ownership and taking day-to-day management roles within their companies. This is certainly true for WCD respondents. They come generally from highly controlled family businesses, where ownership and management are firmly in family hands. Their governance structure is less formal and, not surprisingly, strongly influenced by family.

KPMG Global Family Business Survey

Family business respondents in the Global Survey are less 'close' to the founding family.

- Three-fourths (76 percent) are companies where the family holds the majority stake of the business, though in only 42 percent, the ownership is 100 percent.
- The CEO is a family member in 71 percent of the surveyed companies and in 52 percent of cases less than half or none of the board is made up of family members.
- Half of the respondents have a formal governance structure with the board of directors and an additional 20 percent have a less formal structure with the advisory board.

Throughout their growth and development, family businesses view family control and leadership as an integral part of their business strategy. The vast majority of WCD Survey respondents (90 percent) report that the family holds a majority stake in their company, wherein 74 percent represent families owning 100 percent of the business, which gives family members ultimate control over company direction (Figure 1).

Furthermore, family plays a dominant role in decision-making and business management: in 89 percent of the cases, the CEO is a family member, thereby leaving control over business in the hands of the family business (Figure 2).

FIGURE 1 What proportion of the company is owned by family members?

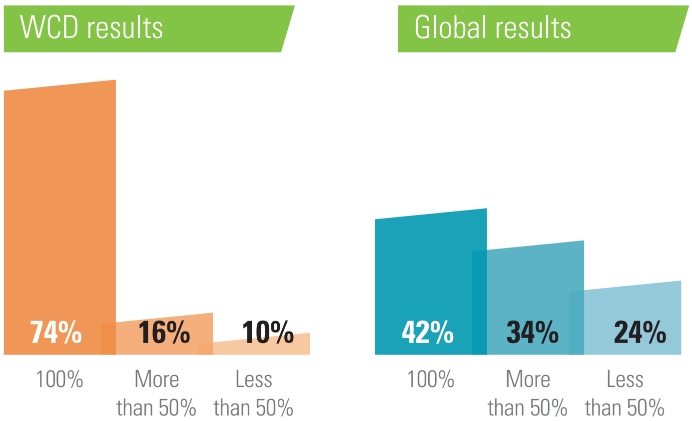
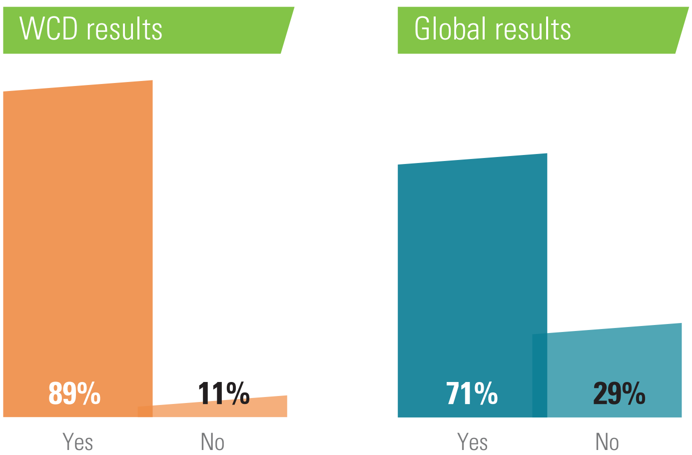


FIGURE 2 Is the CEO of the business a member of the family?



Source: WCD Family Business survey

This figure is even higher and reaches 100 percent in companies not fully owned by family members.

An additional detail to the profile of the family businesses surveyed is their predominantly informal governance structure: only one-third of companies (37 percent) have a formal structure with a board of directors and 11 percent mention a less formal structure with the advisory board (Figure 3). Moreover, almost two-thirds (68 percent) report that more than half or their board is made up of family members (Figure 4).

FIGURE 3 Please select the option that best describes your governance structure.

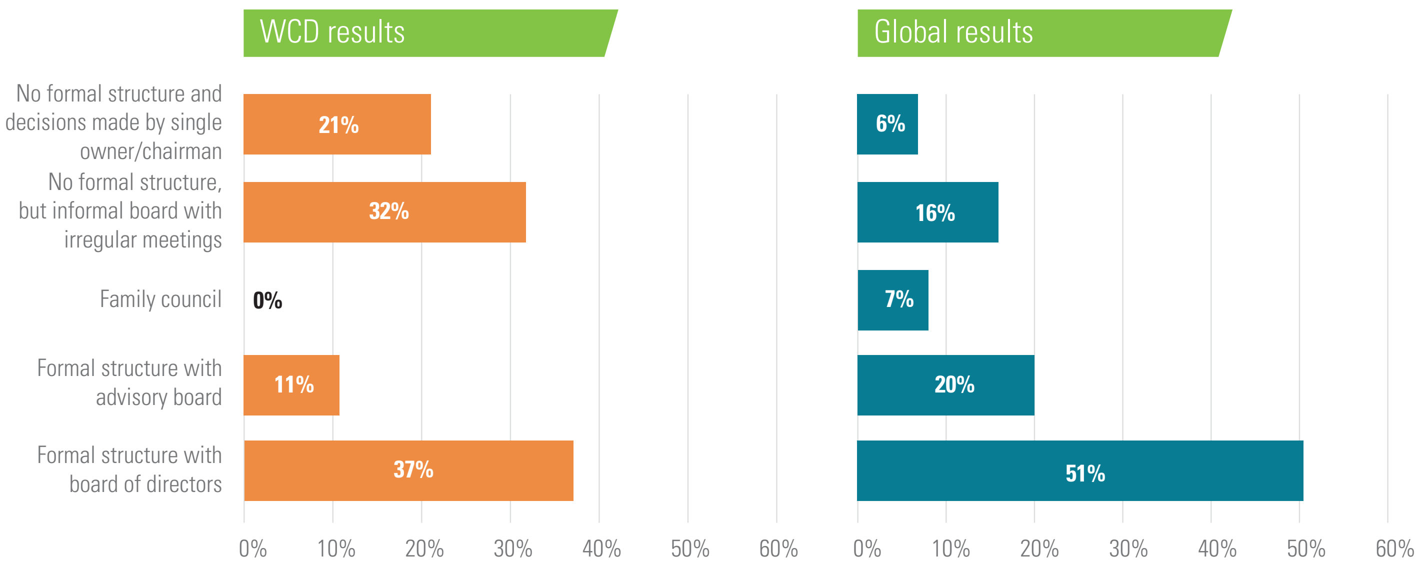
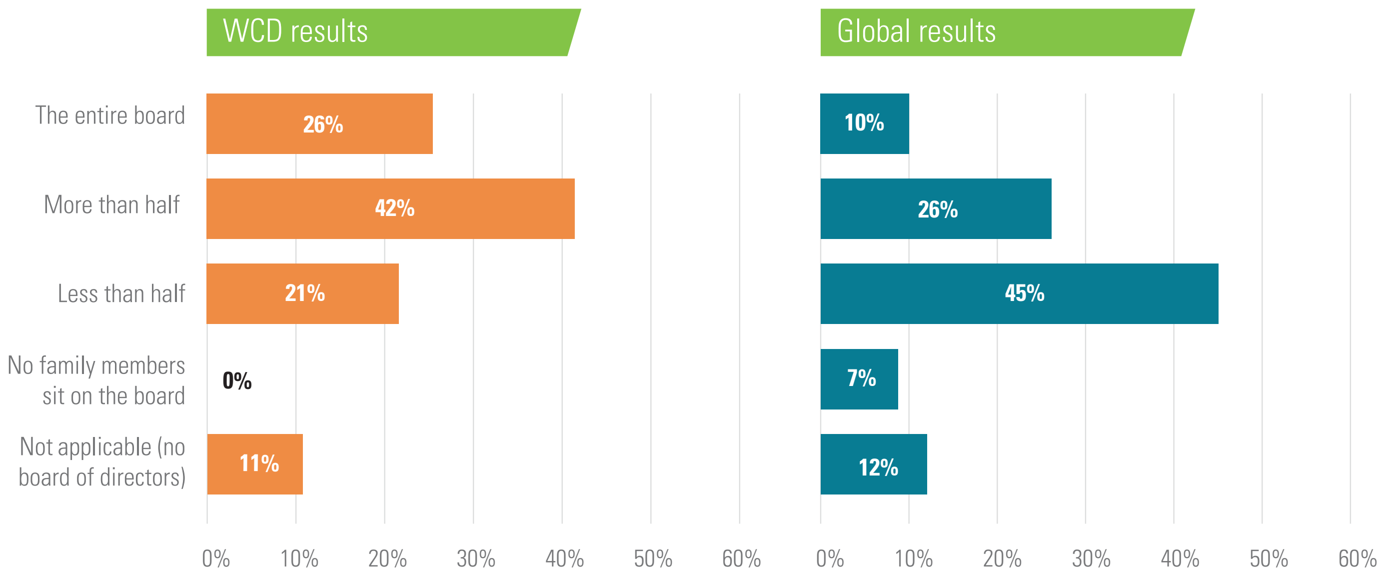


FIGURE 4 What proportion of the board of directors is made up of family members?

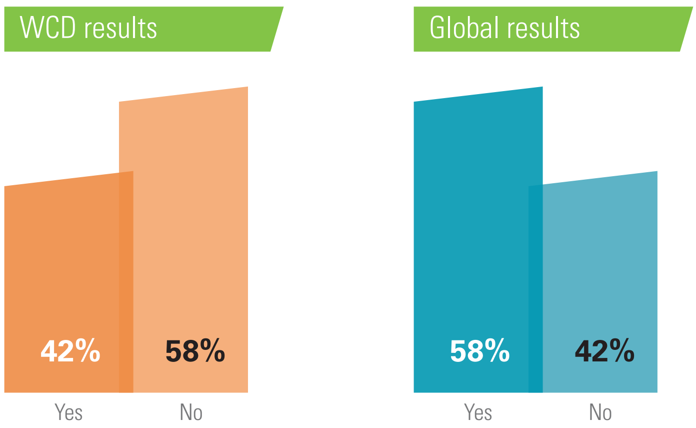


Source: WCD Family Business survey

Growth strategies and financing needs

Finance plays a key role in funding growth and expansion plans. In family businesses, the need for control, long-term orientation and a desire for discretion make it challenging to find an appropriate financing partner. The vast majority of WCD members surveyed are keen, even more than others, to use traditional sources of financing that enable them to maintain family control: own profits and bank debt, neglecting other financial options available to them.

FIGURE 5 **Are you currently seeking external financing for your projects?**



Source: WCD Family Business survey

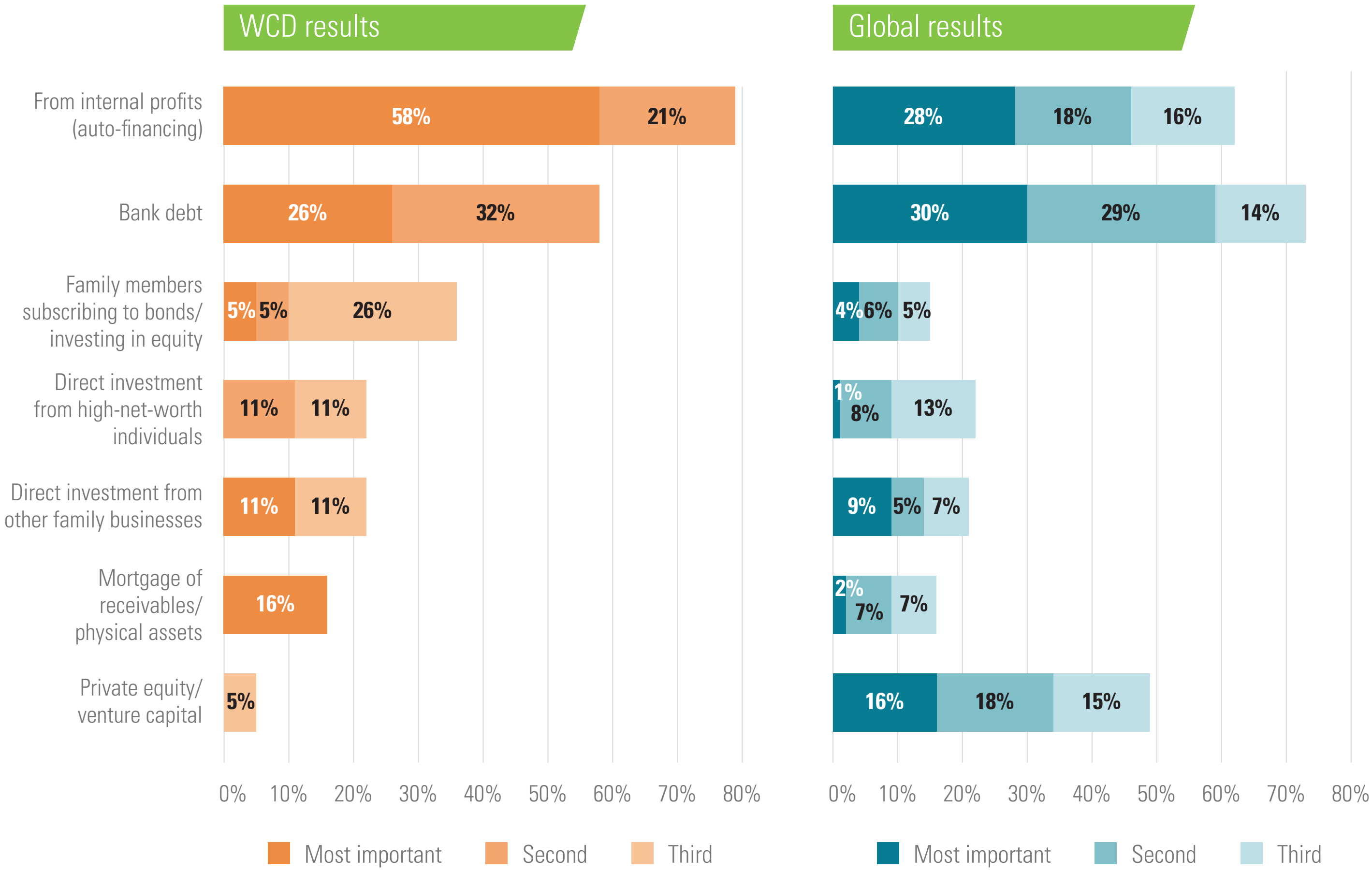
Like any other businesses, family companies need financing and 42 percent of those surveyed are currently seeking outside financing confirming this fact (Figure 5). Our respondents further prove the general research of family businesses that they are largely self-financed, with 79 percent preferring financing through their own profits where possible (Figure 6). It is not surprising then that an alternative to internal profits is another traditional funding source — bank debt, mentioned by 58 percent of respondents. This choice is enhanced by the obviously negligible impact of the current economic climate on the ability of family businesses to finance their growth through bank loans, with only 16 percent of respondents characterizing such impact as significant or very significant (Figure 7).

Family businesses are ready for quick and ambitious growth, identifying acquisitions as one of their main drivers for external financing in both the short-to-medium (58 percent) and in the long (53 percent) term (Figures 8 and 9). Other financing priorities are expansion in new geographical markets, new product or services, organic growth, and, not surprisingly, day-to-day operations within the next 1–3 years.

KPMG Global Family Business Survey

While the preferred sources of financing stay the same — bank loans and retained earnings — the Global Survey respondents seem to be more dependent on external financing: 58 percent of them express a need for external financing for their growth projects.
They also seem less ambitious and adventurous, at least in the short term, as they plan acquisitions and development in new geographies mostly in the distant future.

FIGURE 6 **How does your family business usually finance its projects?**



Source: WCD Family Business survey

FIGURE 7 **Has the current economic climate influenced your ability to finance your projects via bank loans?**

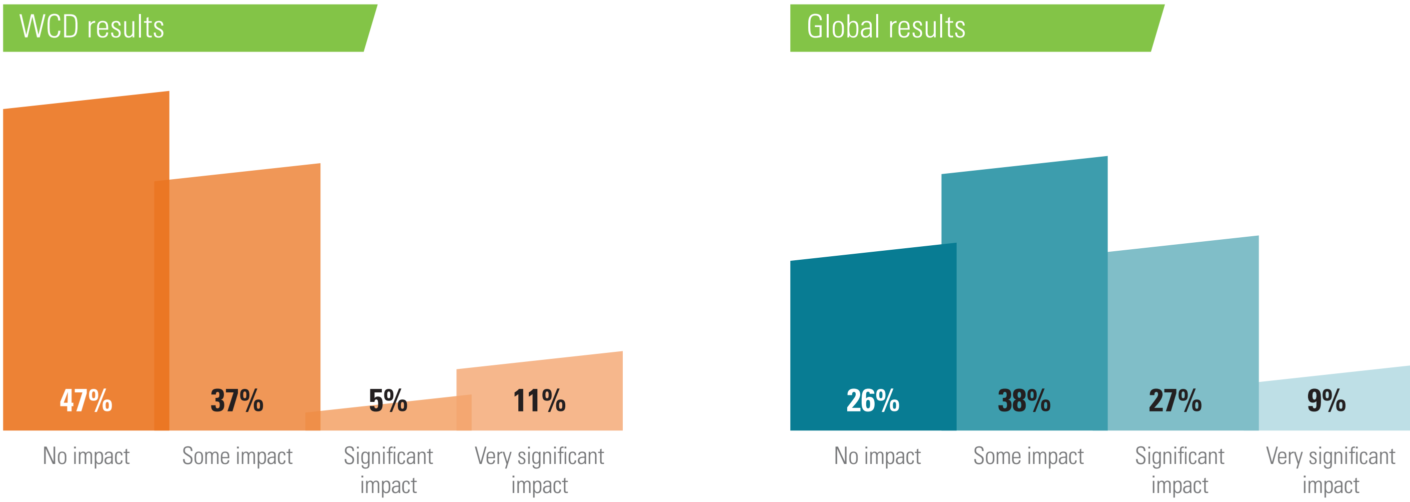
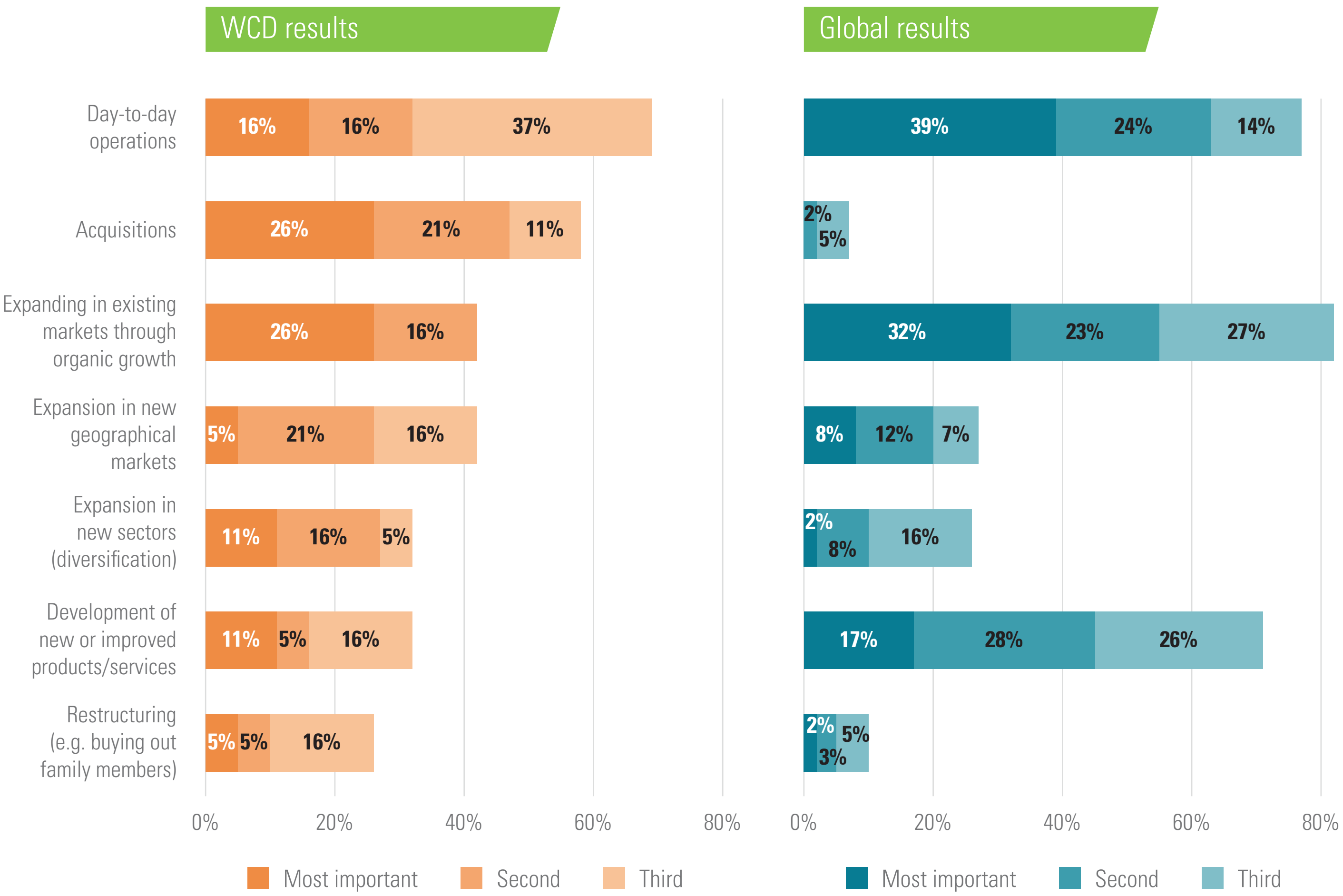
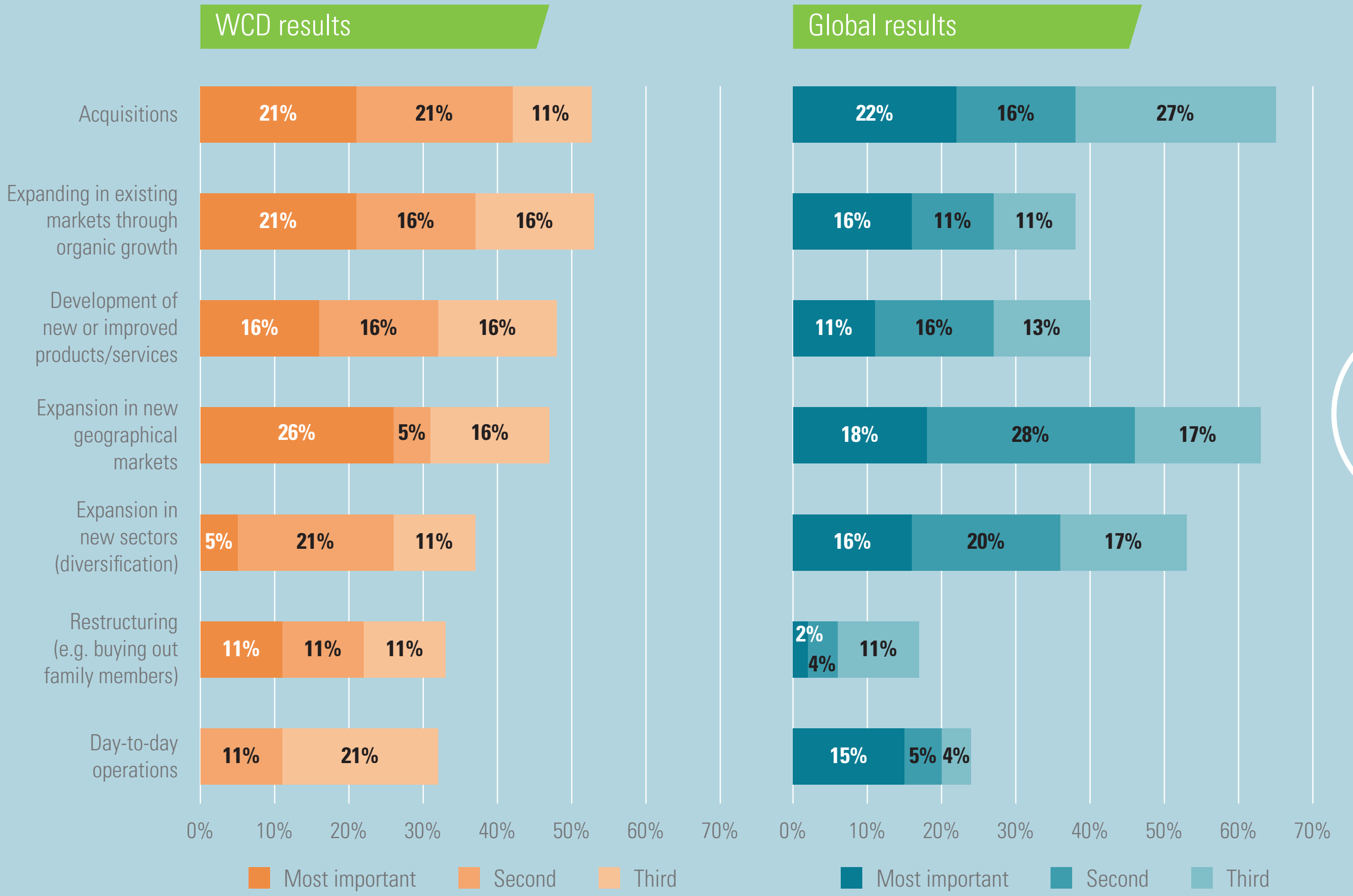


FIGURE 8 **What is likely to drive your need for external financing in the short/ medium term (1-3 years)?**



Source: WCD Family Business survey

FIGURE 9 **What is likely to drive your need for external financing in the long term (3+ years)?**



Source: WCD Family Business survey

Independence is key

In their pursuit of sustainable growth, family businesses try to balance their financing needs with a reluctance to relinquish control and a desire for independence. Striving for further development and asset growth, they are ready to crack open their capital to the right investors, always carefully guarding their independence.

While family businesses often steer away from equity financing aimed at retaining ownership of the company, some of them take external financing in order to further achieve their potential. Survey results suggest that family businesses are increasingly ready to open their capital, especially in the long-term perspective. Although only 32 percent of the surveyed companies have previously offered equity to external investors to allow them to pursue their strategy (Figure 10), 37 percent would consider this opportunity in the short-to-medium term and almost two-thirds (63 percent) say they would be willing to give up equity over the long term (Figure 11).

FIGURE 10 In the past, have you ever offered equity in the business to external investors to pursue your strategy?

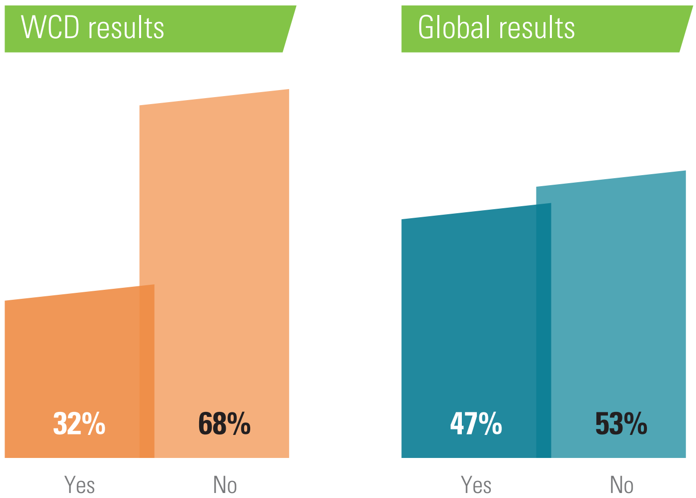
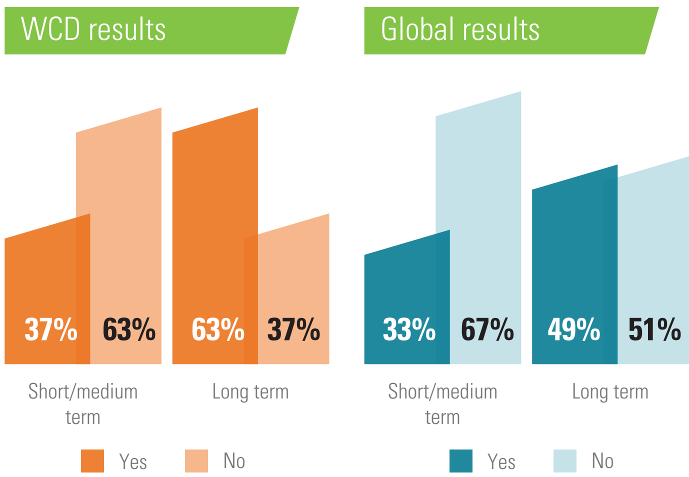


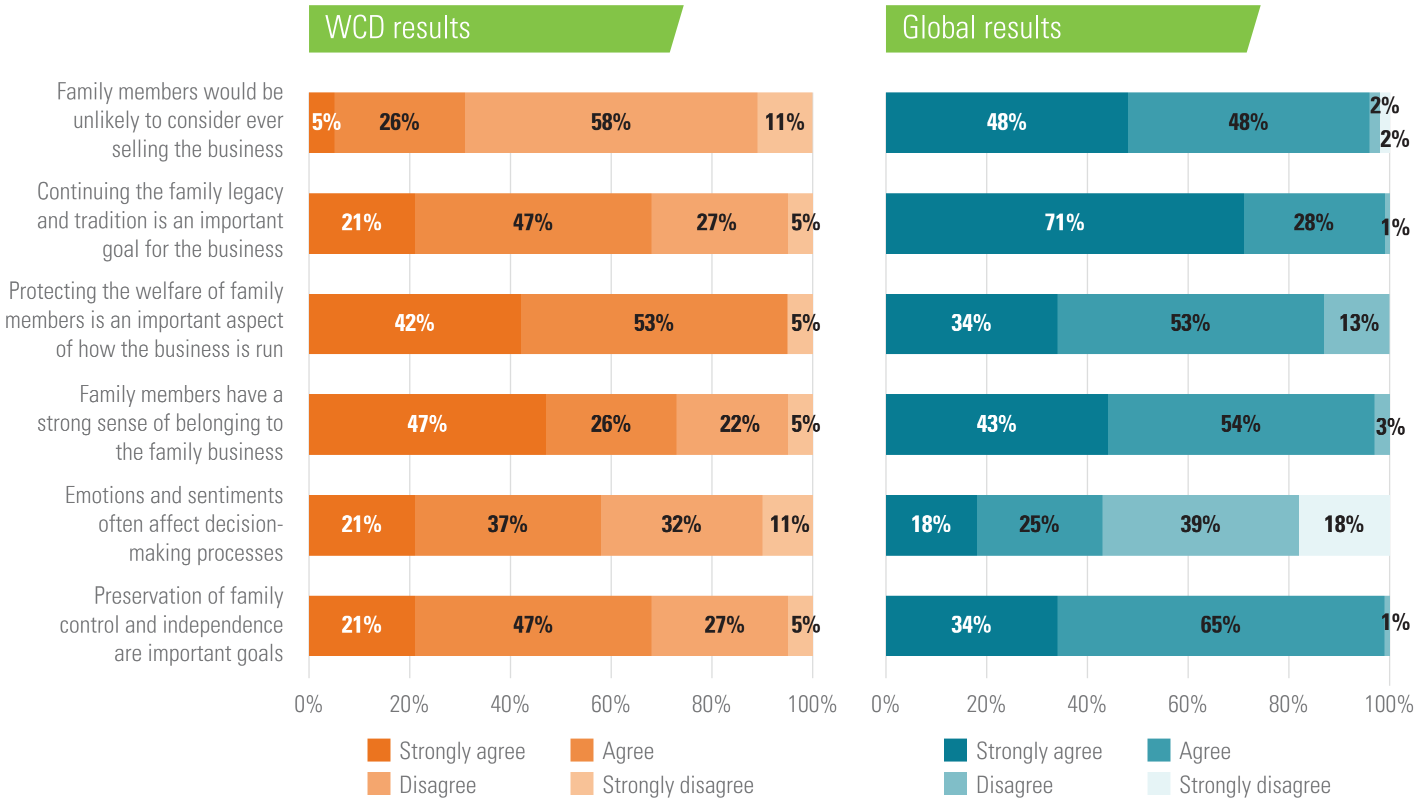
FIGURE 11 In the future, would you consider offering equity in the business to pursue your strategy?



Source: WCD Family Business survey

Is retaining capital really crucial for family businesses? The answer is not black and white anymore with one-third of the respondents (32 percent) not considering the preservation of family control as an important goal, and another two-thirds (69 percent) indicate family members' potential readiness to sell the business in the future (Figure 12).

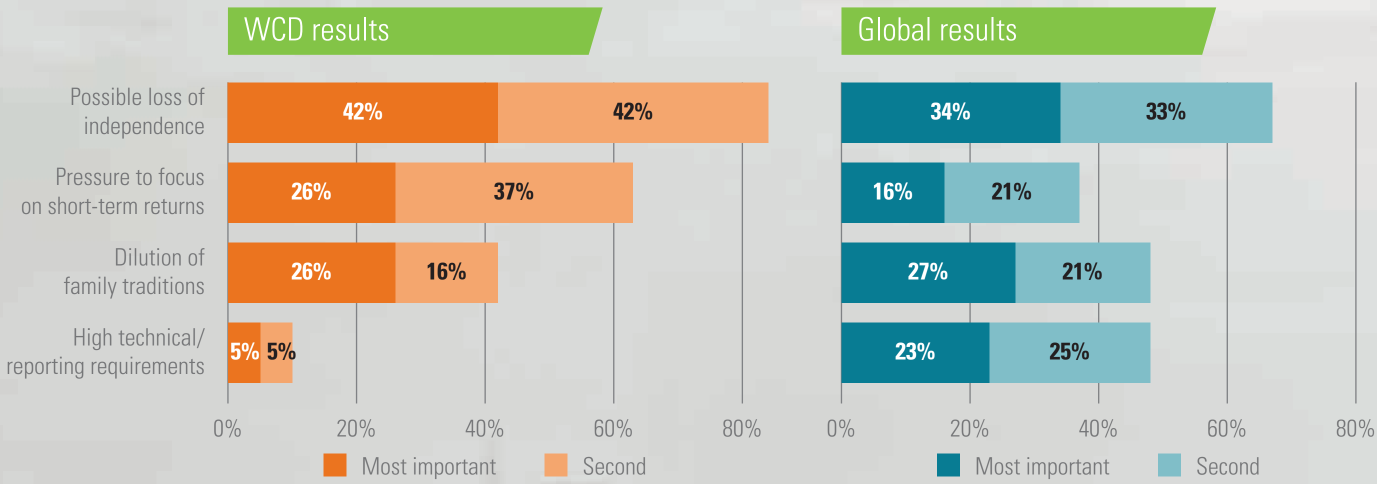
FIGURE 12 Please select your level of agreement with the following statements



Source: WCD Family Business survey

Willingness to open capital for additional funding by no means signifies that family business owners are willing to lose their control over the business. The most important barrier that would prevent firms from offering equity is the possible loss of independence, outlined by 84 percent of respondents (Figure 13). This is further strengthened by the fact that 68 percent of those surveyed consider preservation of family control and independence as important goals (Figure 12). Long-term focus in managing the family business makes an additional 63 percent of respondents wary of the potential external investors' pressure on short-term returns.

FIGURE 13 **What factors might prevent you from offering equity in the business?**



Source: WCD Family Business survey

KPMG Global Family Business Survey

The Global Survey respondents are, similarly to WCD members, ready to consider offering equity to the right investors and almost half of them (47 percent) have had such experience in the past.

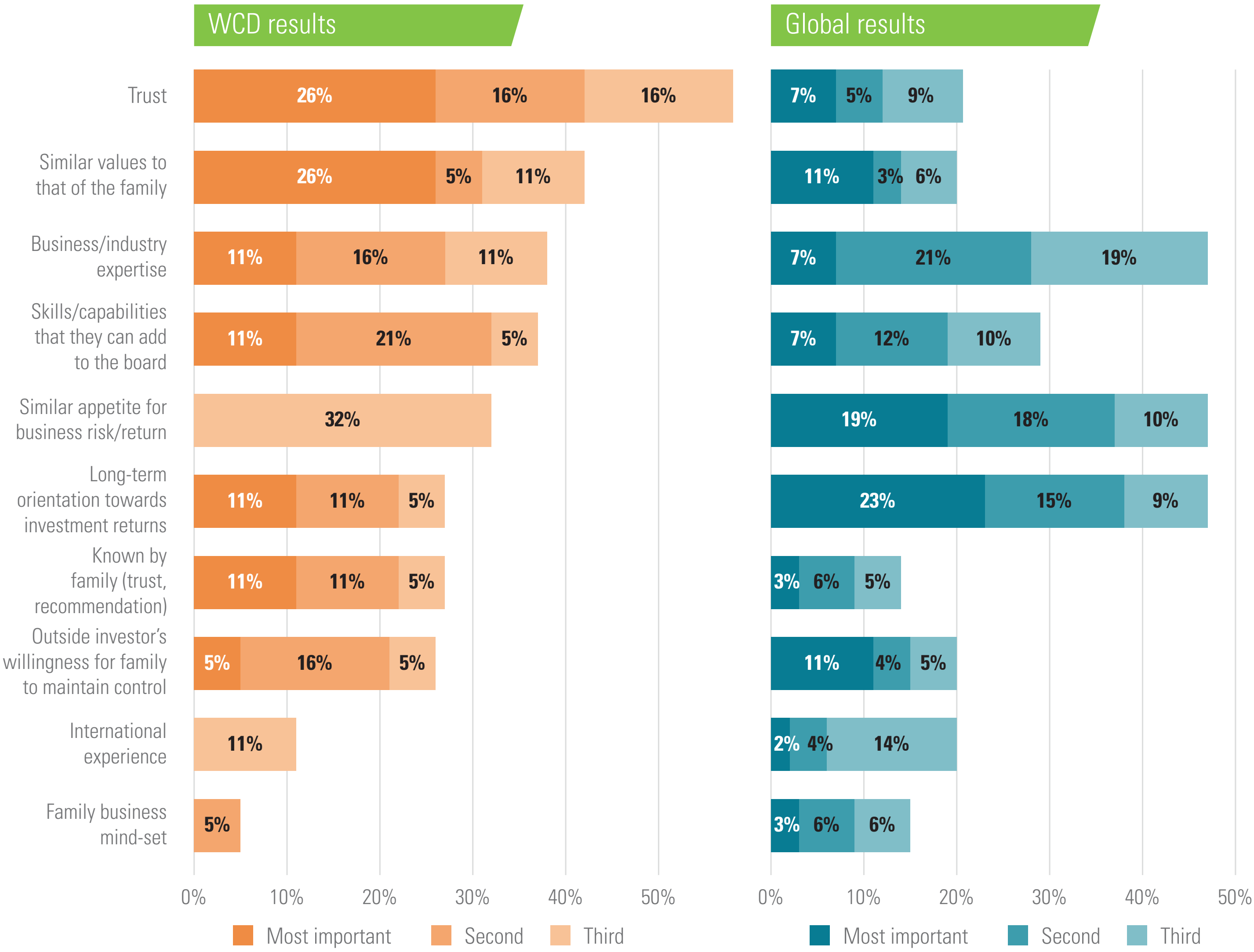
Indeed, they are even more focused on retaining equity and independence: 96 percent state that family members are unlikely to ever sell the business, and 99 percent agree that preserving family control and independence are important goals.

Focus on family values and additional expertise

WCD's surveyed family businesses are clear on what drives their success and place importance on the family element, namely shared values, ethos and other intangible assets. They recognize that preservation of family values should not prohibit them from an outside investor, acknowledging the benefits they could bring to their business.

Family culture and values are the cornerstones of family businesses' growth and business strategies. When asked to rate the desired characteristics for external investors, the respondents preferred primarily intangible assets like trust (58 percent) and values similar to those of the family (42 percent) (Figure 14). Closeness to the family and strong family influence common to the surveyed companies has obviously manifested itself in these choices.

FIGURE 14 Assume you are considering raising additional capital by issuing equity. What characteristics are/would be important to you?



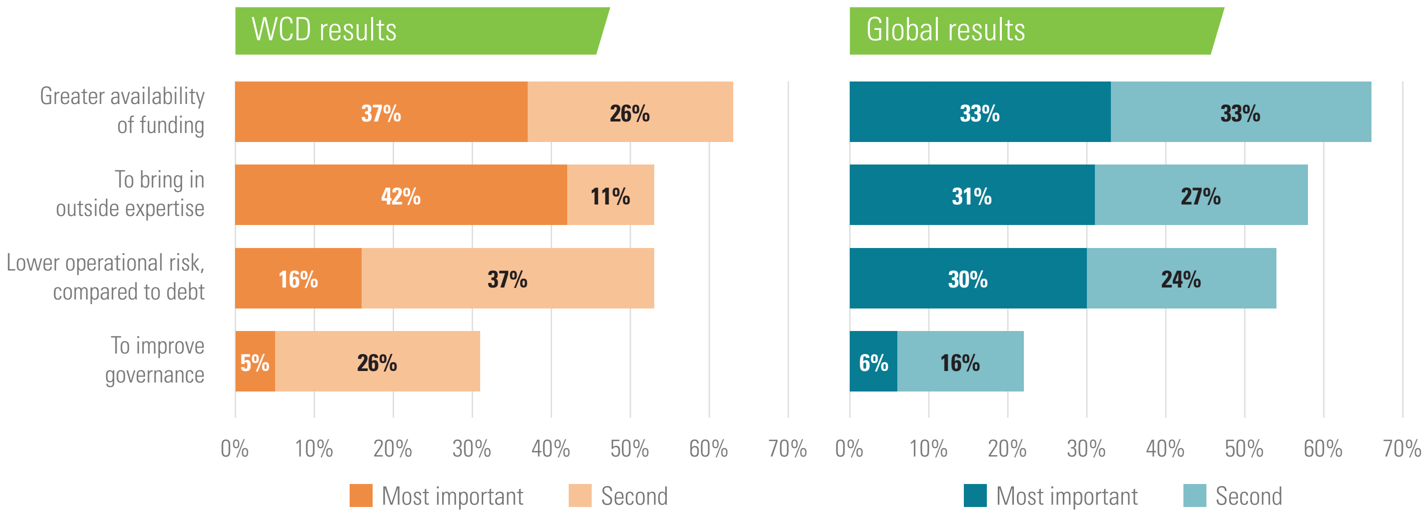
Source: WCD Family Business survey

While greater access to funding is the first reason for family businesses to offer equity in their company, they are also attracted by the additional expertise an outside investor can bring: 53 percent consider this factor important, including 42 percent describing it as the most important (Figure 15). On top of this, skills and capabilities that external investors can add to the board and their business and industry knowledge are cited by 38 percent and 37 percent of respondents, respectively, placing them in the top three of the most desired characteristics, after similar values and trust (Figure 14).

The vast majority of respondents realize the value investors could bring and would want them to play an important role, among them 47 percent are looking forward to the investors' advice and expertise and another 37 percent are prepared for investors to take a board seat. Only 16 percent say they would want outside investors to stay completely passive (Figure 16).

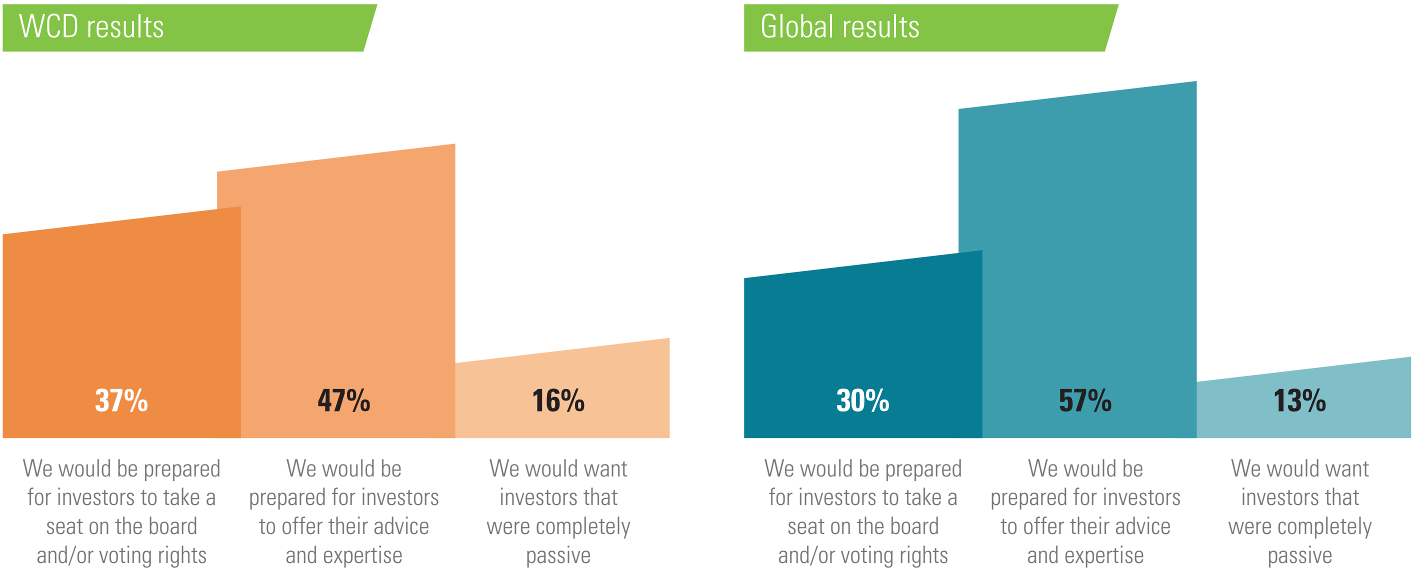
Focus on family values and intangible assets and an appetite for external knowledge and experience are clearly reflected in the family businesses' choice of desired investors. Corporate investors with industry expertise are on the top of the agenda for WCD family businesses, chosen by 84 percent of respondents. Other desirable investors are HNWIs, cited by two-thirds of respondents (69 percent) and other family businesses, rated high by 53 percent of the surveyed companies (Figure 17). This is significantly higher than in the Global Survey, consistent with the higher focus on 'intangibles'. In parallel, financial investors are hardly considered by WCD family businesses, contrary to the Global Survey.

FIGURE 15 **What factors might encourage you to offer equity in the business?**



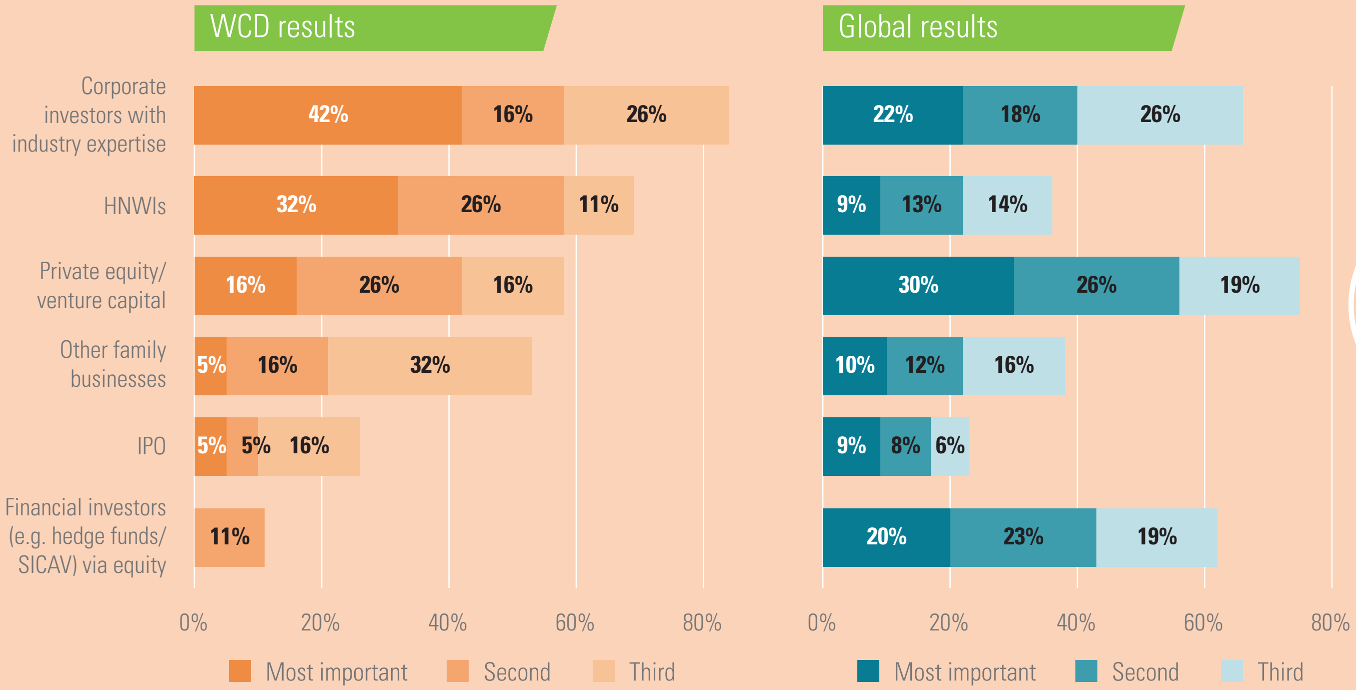
Source: WCD Family Business survey

FIGURE 16 **Assuming that you were interested in opening your capital to external investors, would you want those investors to have an active role?**



Source: WCD Family Business survey

FIGURE 17 Assuming that you were interested in opening your capital to external investors, what type of investors would you prefer?



Source: WCD Family Business survey

KPMG Global Family Business Survey

Like WCD members, the Global Survey respondents placed a high value on investment partners' experience. They rely on the knowledge, skills and industry expertise which external investors can bring and are ready to offer them board seats and voting rights.

What differs, though, in the two samples is that, while prioritizing their expectations for the external investors, companies from the Global Survey seem less focused on intangible assets, like trust and values, and are more focused on long-term orientation and similar appetite for risks and returns. The lower importance given to intangible issues may reflect a desire among many family businesses to balance out family involvement with more objective investors.

Investment opportunities with HNWIs

In their search for investment partners, family businesses place a high importance on shared values and trust, external expertise, long-term perspectives and similar understanding of risks, and most of them believe HNWIs can provide these assets. It is worth noting that a minority of family businesses have already tapped into this type of investment and had difficulty finding a suitable partner. Education may help to alleviate any potential lack of knowledge about the possibilities a partnership between family firms and HNWIs could bring. Family business associations and business incubators could help by facilitating networking and sharing positive experiences.

Survey results show that inside the WCD community, family businesses and HNWIs' relations are largely underestimated and undeveloped: less than a quarter of the surveyed companies (21 percent) have tapped into HNWIs and other family business investment pools in the past (Figure 18).

Interestingly, all of the family businesses that have already attracted HNWIs' funding rate this experience as positive or very positive (Figure 19).

When asked to consider the benefits HNWIs may offer as investment partners, family businesses mention a similar understanding of risks, advice and expertise, and shared values and high level of trust as the most attractive (Figure 20) — all of them are generally expected by a family business from an investor. Half of the family businesses surveyed (52 percent) further agree that HNWIs are patient investors and will not push too hard for an exit (Figure 21).

There is no surprise that as principal barriers to such partnerships, family businesses rate difficulties in finding a suitable partner and their limited availability as high, cited by 74 percent and 42 percent of respondents, respectively, rather than more business-related difficulties that may arise in the course of such a partnership, like complex negotiations, interference with management or an equity issue (Figure 22).

Lack of communication and networking within the family business community may partly explain why the positive experience of HNWIs' funding stays in the shadow. Despite the fact that over half of the surveyed companies

FIGURE 18 Have you previously obtained direct investment from HNWIs or other family businesses?

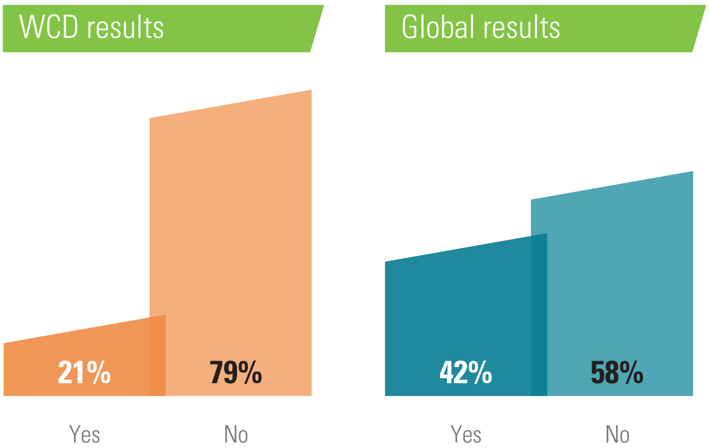
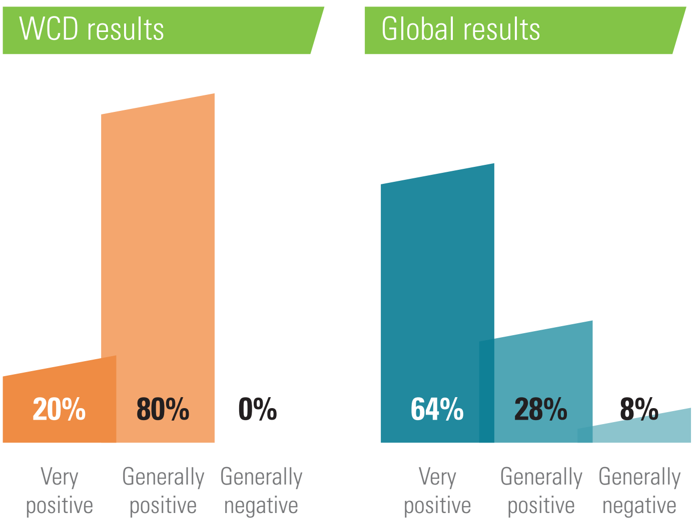


FIGURE 19 How would you rate your experience of receiving finance directly from HNWIs or other family businesses in comparison to financing from other sources?



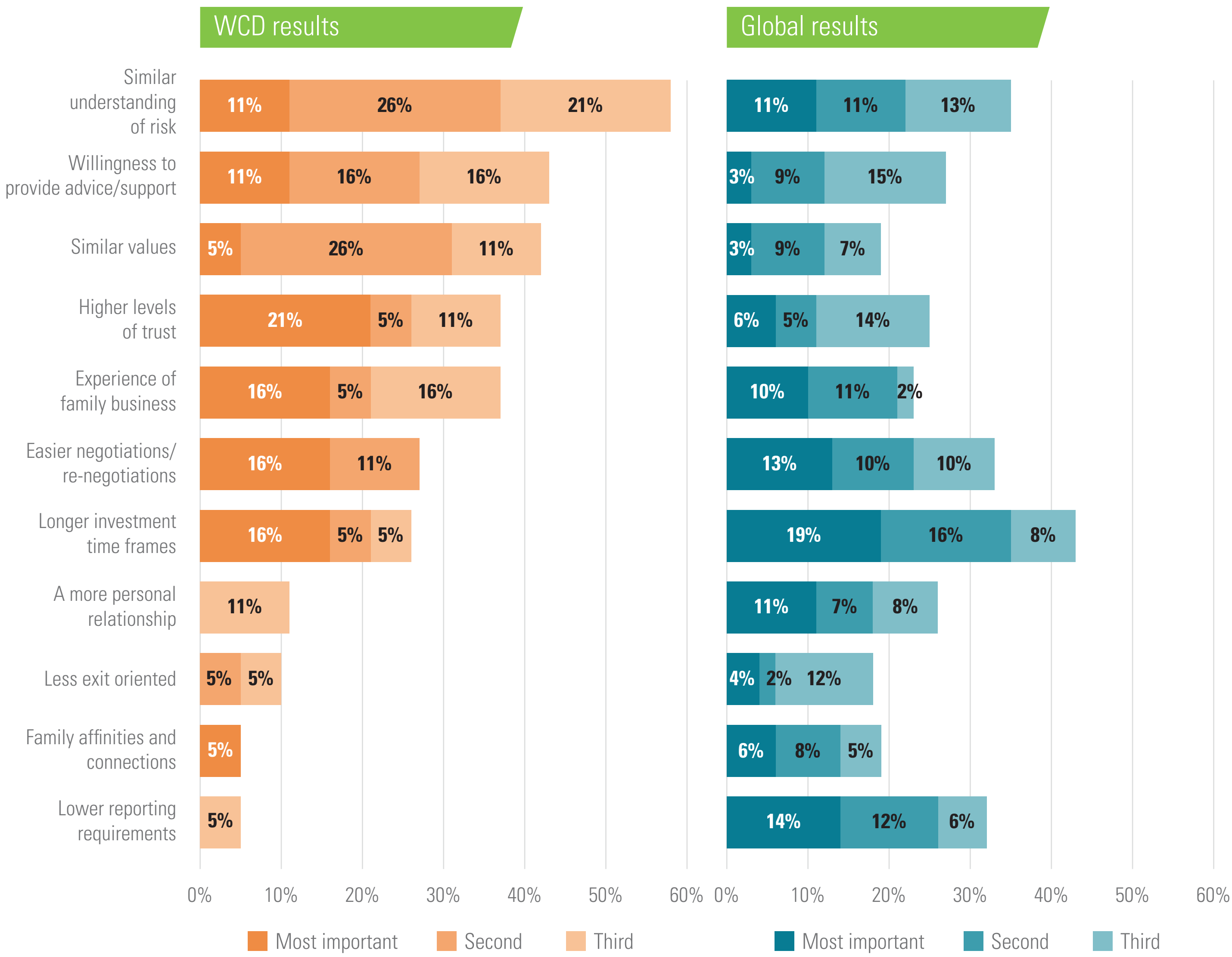
Source: WCD Family Business survey

(58 percent) meet with other family businesses to discuss general business issues and a further 37 percent share their best practices, still almost half of respondents (47 percent) admit to not having many relations with other family firms (Figure 23).

Business consultants, banks and family or friends are named as the most important sources of advice when seeking outside investors (Figure 24).

Hence, the survey results suggest that while many family managers and owners may be open to the idea of bringing

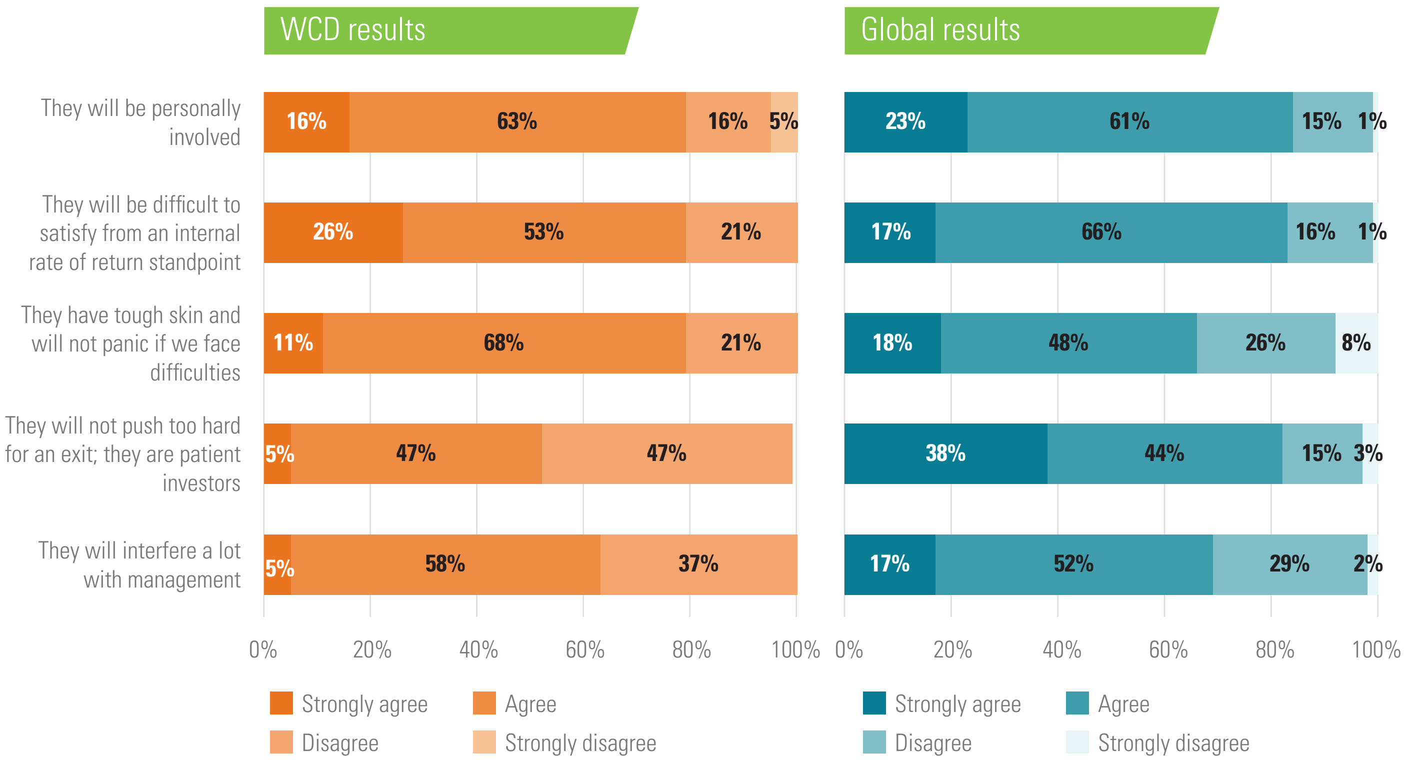
FIGURE 20 What factors might encourage you to source investment from HNWIs or other family businesses as opposed to raising money from more traditional sources like banks or private equity funds?



Source: WCD Family Business survey

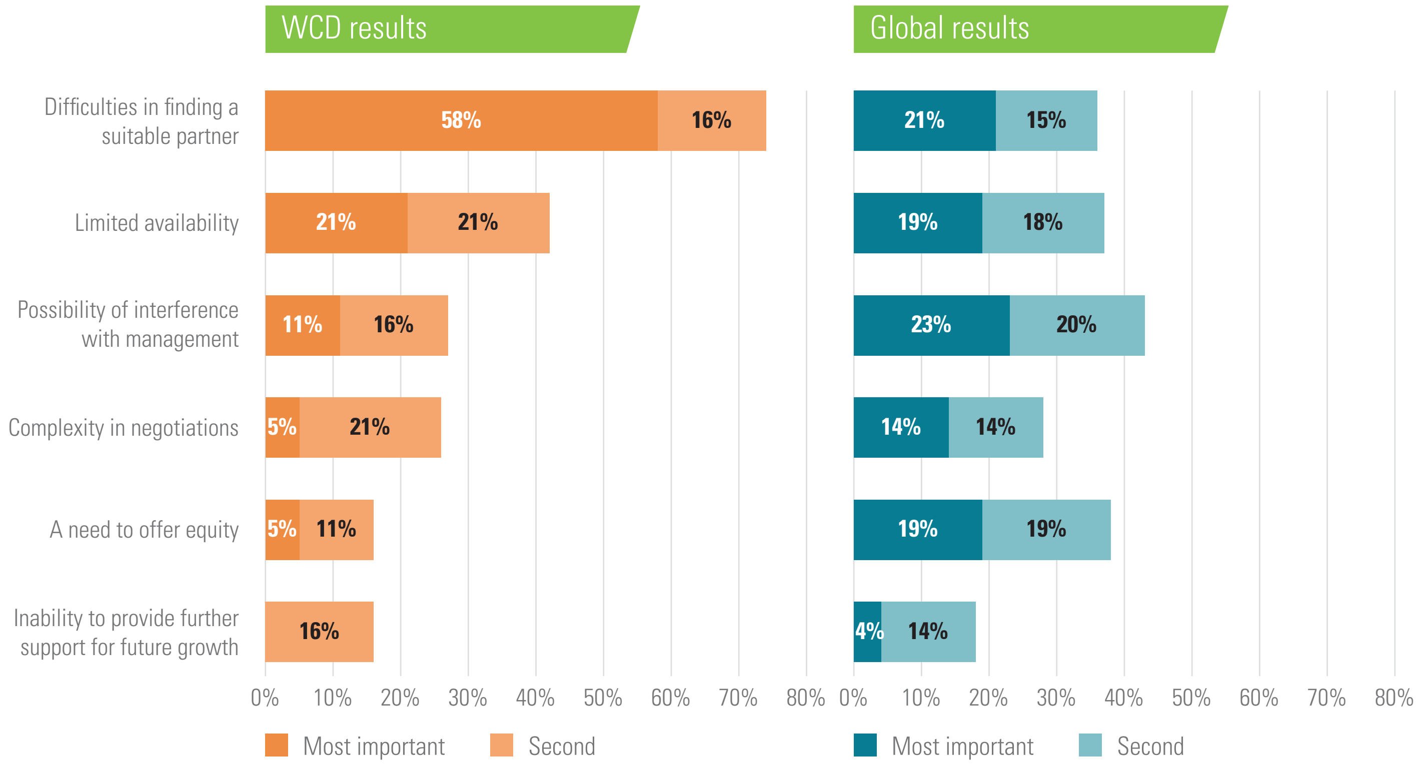
HNWIs and other family businesses in as equity investors, lack of previous experience and communication inside the family business community, as well as difficulties in sourcing this type of capital, are holding them back. The potential for good partnerships clearly exists, and proactive involvement of business consultants and raising the awareness within the family business community will clearly help to bridge the gap.

FIGURE 21 What is your perception of the likely involvement of HNWIs or other family businesses post-investment?



Source: WCD Family Business survey

FIGURE 22 **What do you see as the principal barriers for obtaining investment from HNWIs or other family businesses?**



Source: WCD Family Business survey

KPMG Global Family Business Survey

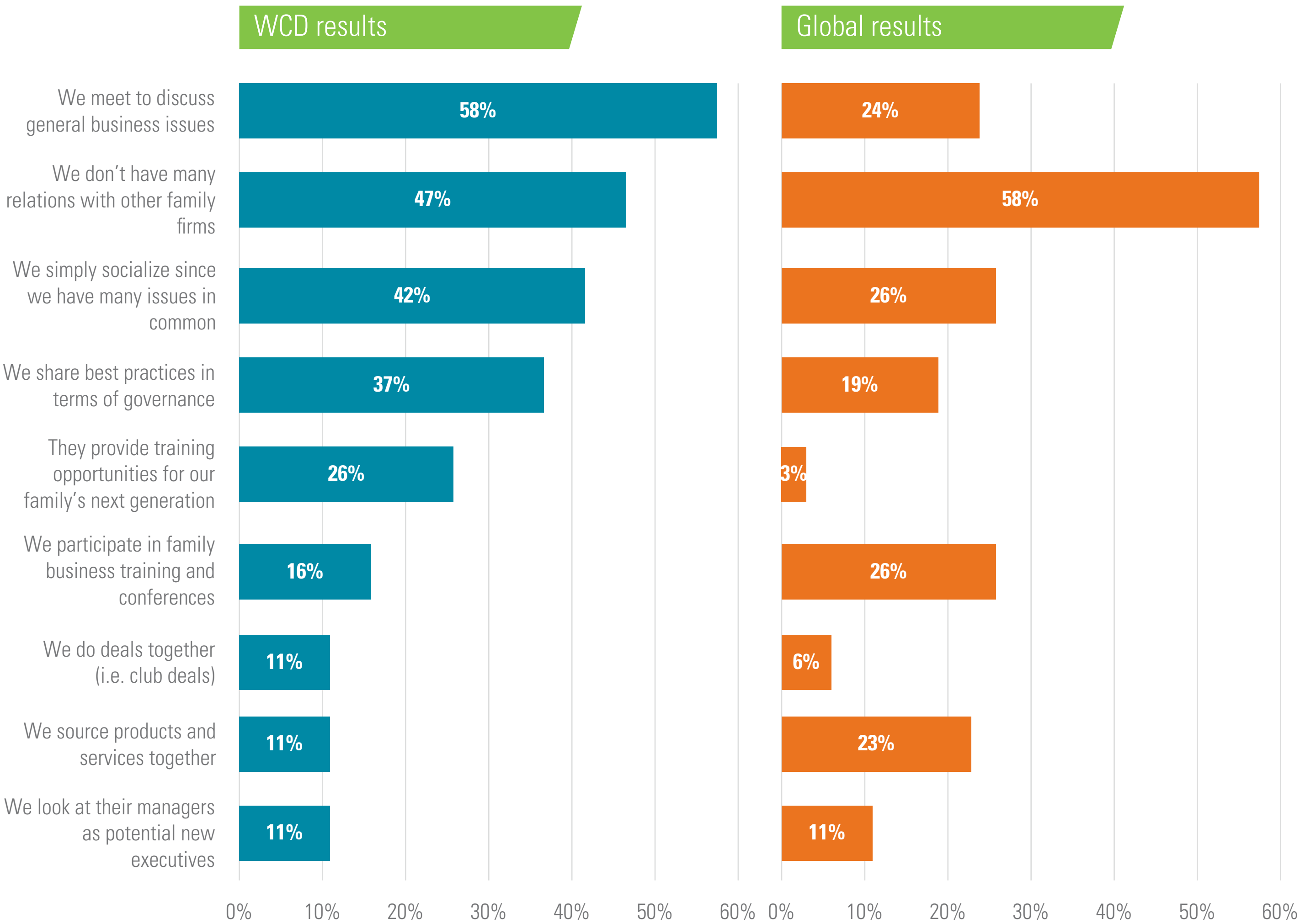
The Global Survey respondents have in general more experience with HNWIs' investments and, similar to WCD members, rate it as highly positive.

Besides the characteristics mentioned by the WCD members, they cite longer investment time frames, easy negotiations and lower reporting requirements as the benefits of HNWIs as investors. This should be taken into consideration by the WCD members considering future funding partnerships.

The Global Survey respondents have even less contact with other family businesses, preferring to approach business consultants and banks for advice. In this regard, WCD seems to be in a favorable position to facilitate networking and experience-sharing among its members.

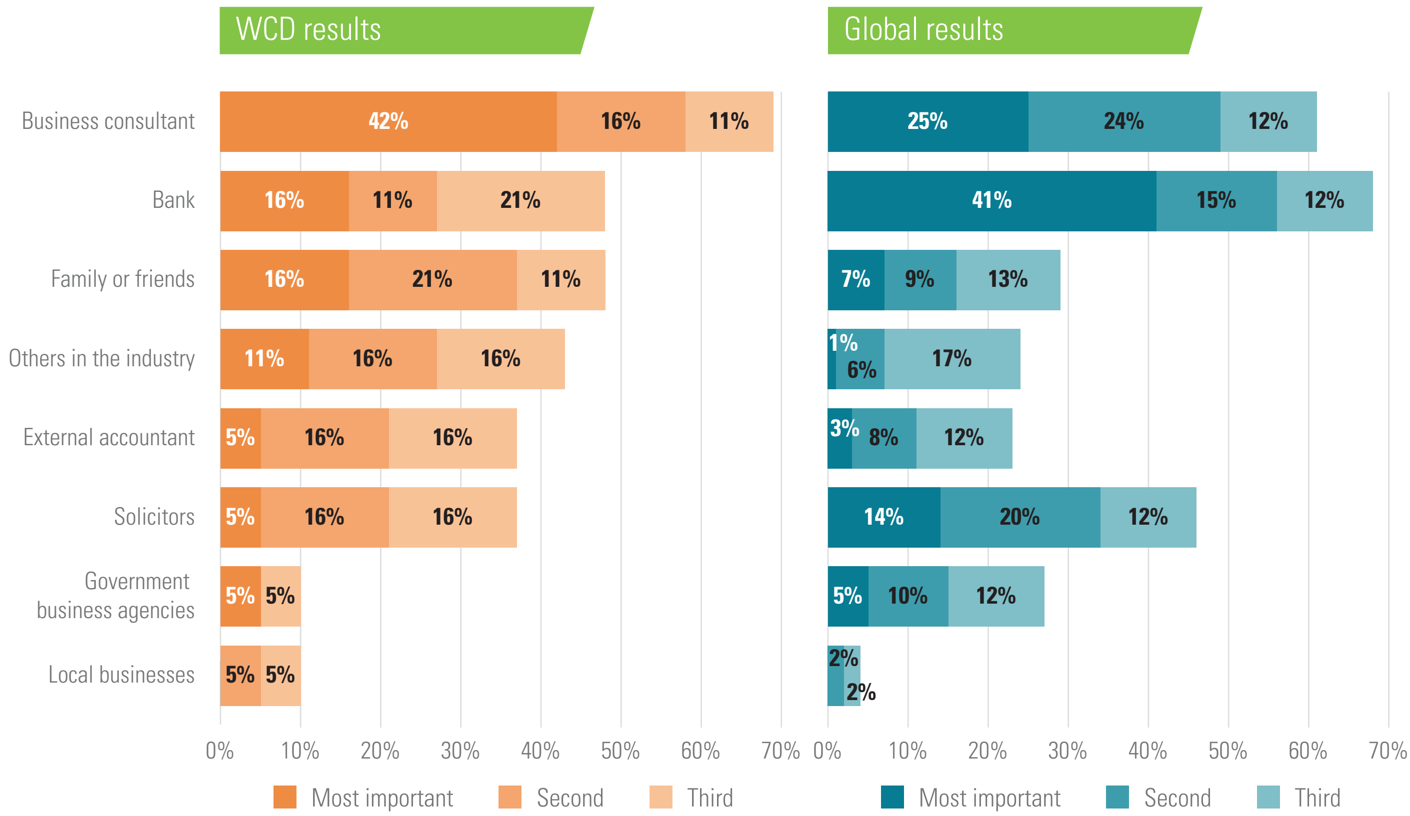
FIGURE 23 **What activities do you have with other family businesses?**

(participants can select multiple options)



Source: WCD Family Business survey

FIGURE 24 If you were looking to bring in outside (non-family) shareholders to raise further capital for the business, who would you approach for advice on how to do this?



Source: WCD Family Business survey

Investment goals of HNWIs

Investment goals of HNWIs

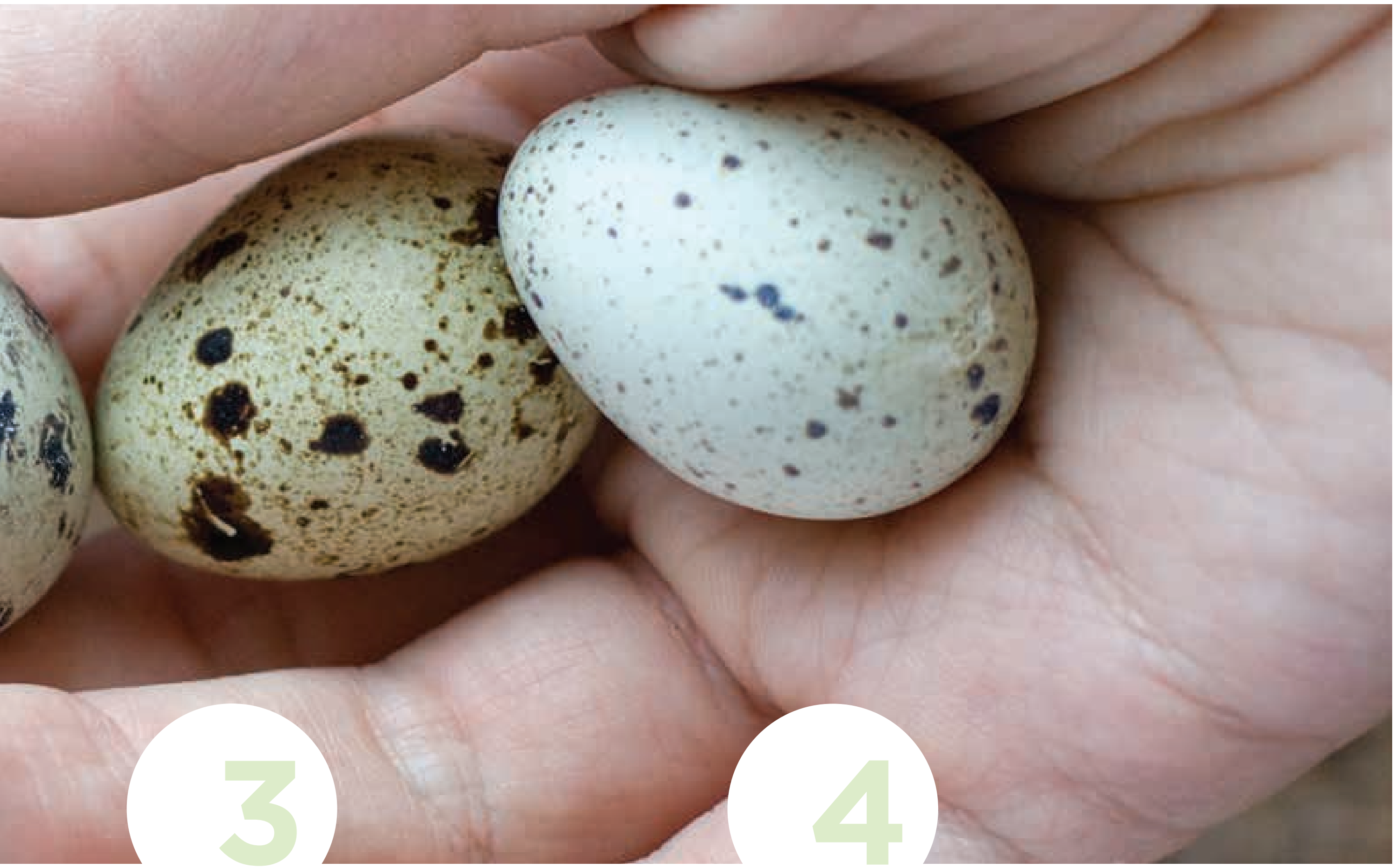
Highlights

1

The majority of WCD HNWIs surveyed have no links with family businesses. They stay actively involved in capital management and, while investing, prefer to regularly express their views and ideas.

2

Long-term capital appreciation, diversification and steady cash flow are the main drivers for HNWIs' investments. When investing directly in other businesses, the surveyed HNWIs prefer start-ups and smaller companies.



3

While WCD HNWIs do not express a particular preference for family businesses, more than half have previously invested in at least one family business and 93 percent of those rate this experience positively.

4

The possibility of family conflicts and unprofessional management are the main reasons that stop HNWIs from investing in a family business.

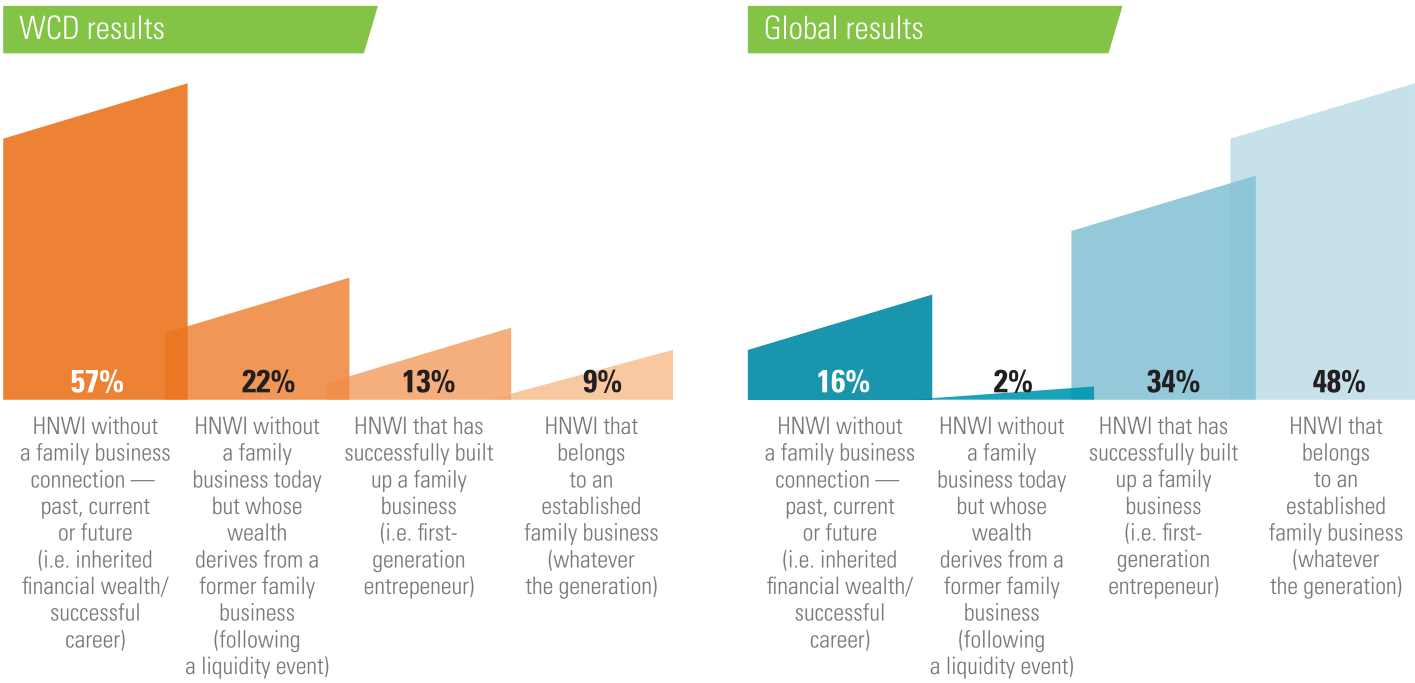
HNWIs are in control of their wealth

The vast majority of HNWIs surveyed have self-made or inherited their wealth and don't owe it to any connections with a family business, neither in the past, nor in the present or in the future. They prefer to stay actively involved in their wealth management and to control their investment portfolios.

More than half of the HNWIs WCD surveyed (57 percent) have no connection to a family business, neither in the past, nor in the present or in the future, and 13 percent are successful entrepreneurs building up a family business in a first generation (Figure 25). The general perception that HNWIs are well-versed in the way family businesses operate, as the source of their wealth is drawn from the family business, may not be the case for our WCD respondents, having in most cases remote relations with family businesses.

HNWIs prefer to stay actively involved in their wealth management and to control their investment portfolios: almost two-thirds of those surveyed (65 percent) control 50 percent or more of their investments; just 9 percent outsource all of their investments to third parties (Figure 26). This high level of involvement is further reflected in the fact that none of the HNWIs surveyed use a family office, suggesting a less formal and more individual approach to wealth management (Figure 27).

FIGURE 25 **Is your wealth connected to a current/former family business?**



Source: WCD Family Business survey

FIGURE 26 To what extent are you managing your wealth yourself?

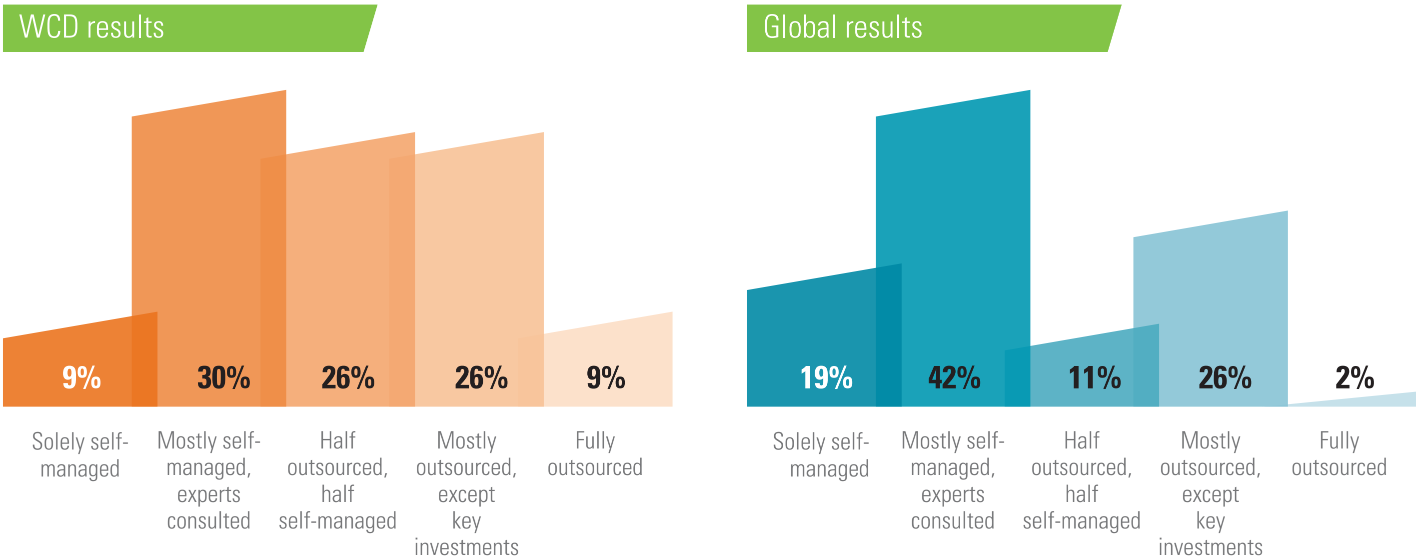
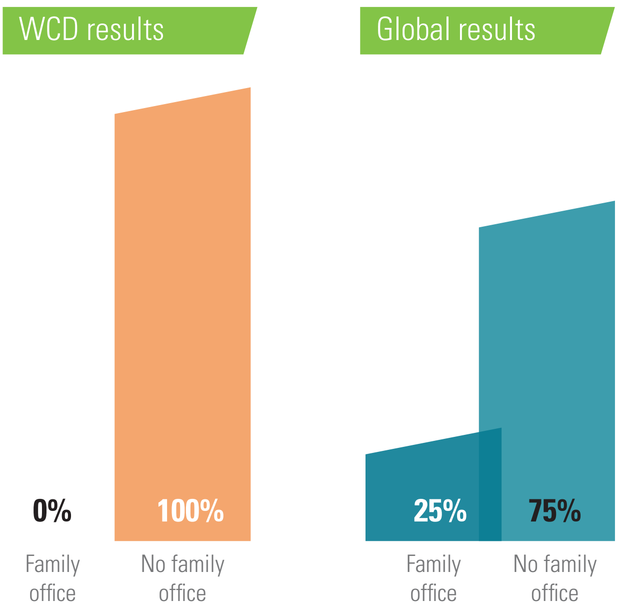


FIGURE 27 Do you manage your investments through a family office?



Source: WCD Family Business survey

KPMG Global Family Business Survey

The HNWIs from the Global Survey differ considerably from the surveyed WCD respondents. The vast majority have direct experience with family businesses: nearly half (48 percent) belong to an established family business that has been in operation for more than one generation and over a third (34 percent) have grown a family business themselves.

Similar to WCD respondents, they like to take responsibility for their investment portfolios: 72 percent self manage

50 percent or more of their wealth and only a quarter use a family office.

Desire for long-term capital appreciation and diversification

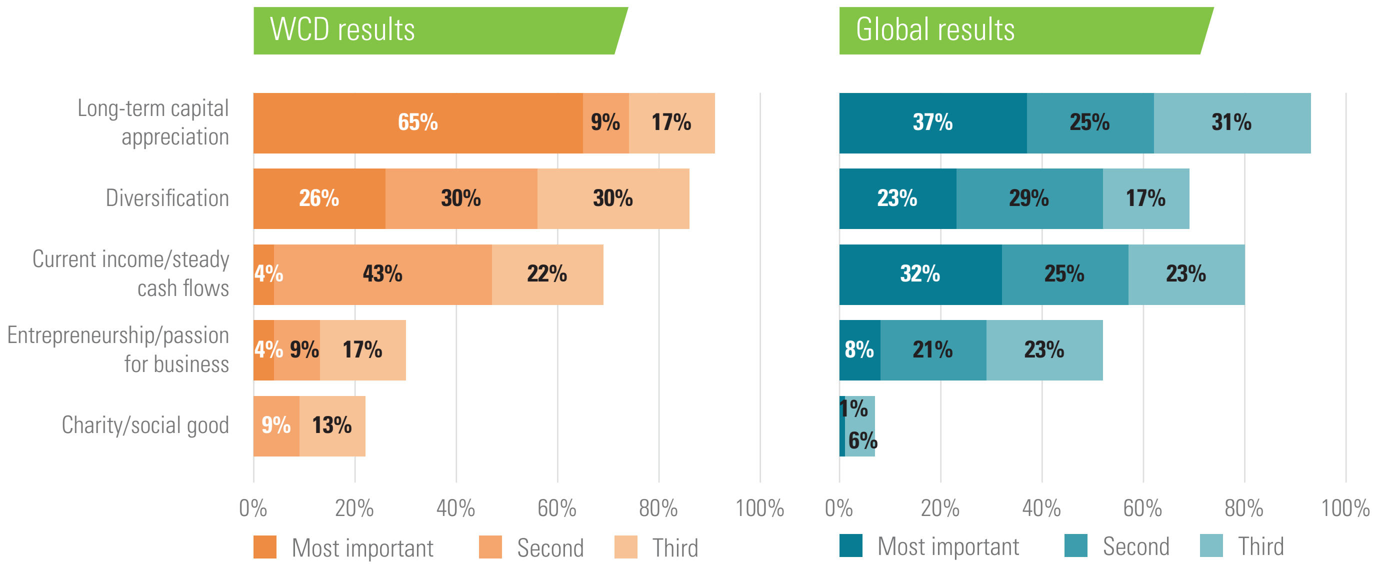
HNWIs are active investors and two-thirds currently invest directly in companies. Moreover, they are patient investors, and in striving for long-term capital appreciation, diversification and stable cash flow, they choose to take on a medium amount of risk in the hopes of generating medium returns. HNWIs seek to deploy their capital in opportunities that answer their demands, i.e. provide long-term returns and significant potential for capital growth, and offer diversification benefits. They opt for start-ups and small companies.

HNWIs invest for three main purposes: long-term capital appreciation ranks first, followed by diversification and current income (Figure 28). The desire of HNWIs for long-term capital appreciation is reflected in their appetite for risk. The vast majority of those surveyed (87 percent) take a balanced approach to risk for investments outside of their main business, searching for reasonable risks with reasonable returns (Figure 29). Indeed, HNWIs are patient investors ready to wait for their returns.

The desire for capital appreciation and diversification balanced with income and portfolio stability explains the HNWIs investment preferences. The survey respondents tend to invest in rather traditional wealth management tools: 100 percent invest in listed equities, followed by 95 percent who invest in real estate and 80 percent in bonds. Direct investment in businesses, though cited by slightly more than half of respondents (52 percent), is only fifth in the rating of committed investments by HNWIs overall (Figure 30).

When asked about their current involvement in direct investments, two-thirds of respondents (65 percent) answered positively (Figure 31) and, consistent with the

FIGURE 28 **Not including investments in your own company, which of the following items are the main driver for investments?**



Source: WCD Family Business survey

desire for diversification and moderate risks, 61 percent outlined their preference for multiple and smaller investments rather than to more rare and more significant ones (Figure 32). The respondents target largely start-ups (93 percent) and small companies (47 percent), with a much lower number of those investing in mid-sized and large companies (Figure 33).

FIGURE 29 **Not including investments in your own company, to what extent are you willing to risk your invested capital when making investments?**

Source: WCD Family Business survey

KPMG Global Family Business Survey

The investment profile of the HNWIs from the Global Survey is similar to the one from the WCD Survey with a bigger appetite for entrepreneurship and direct investment in companies.

They look for long-term capital appreciation, current income and diversification, plus moderate risks combined with moderate returns.

For direct investments, their preferences are shifted to mid-sized and small companies rather than start-ups, which can offer HNWIs the potential for a degree of stability but also rapid growth.

FIGURE 30 **Not including investments in your own company, please rank your committed investments to the following types of investment**
(participants can rank up to seven options)

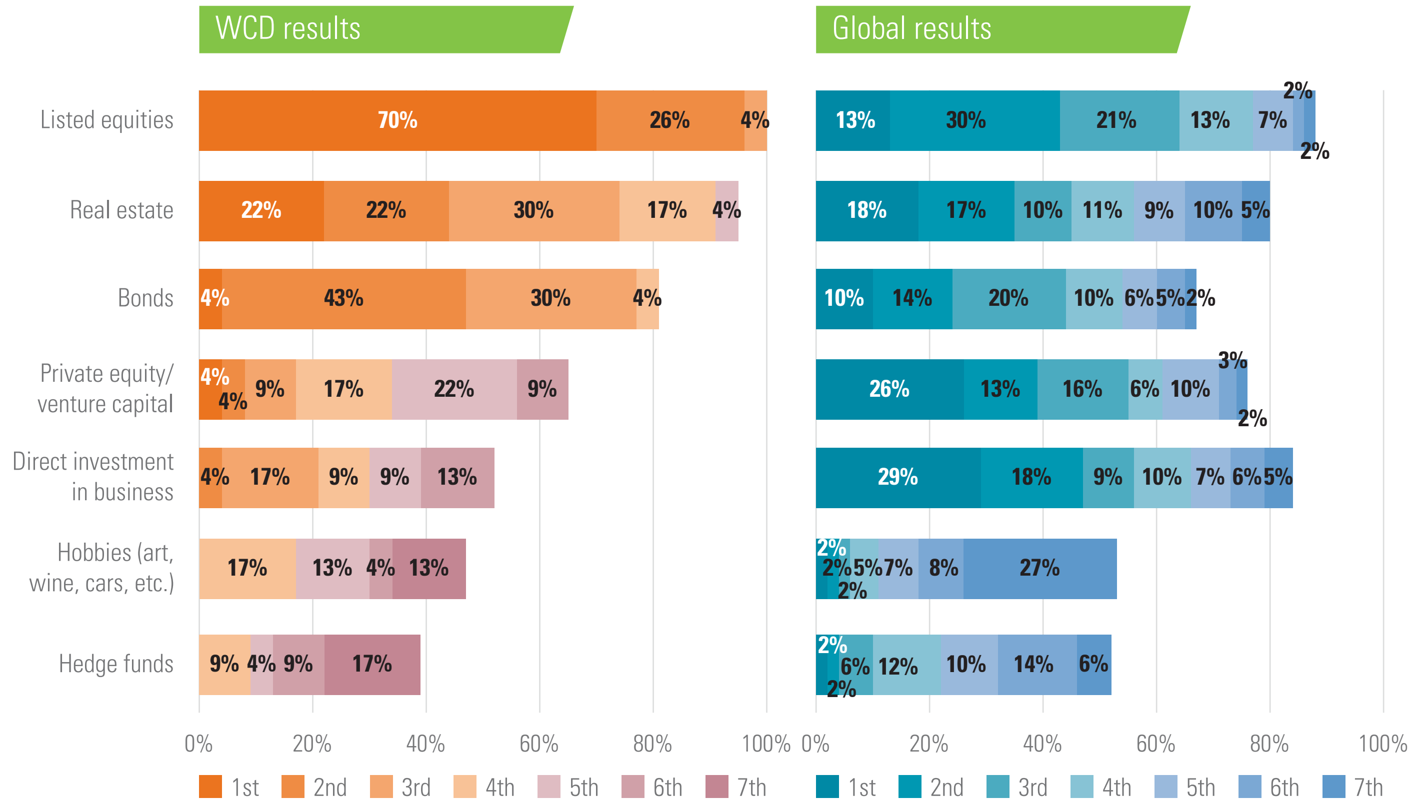
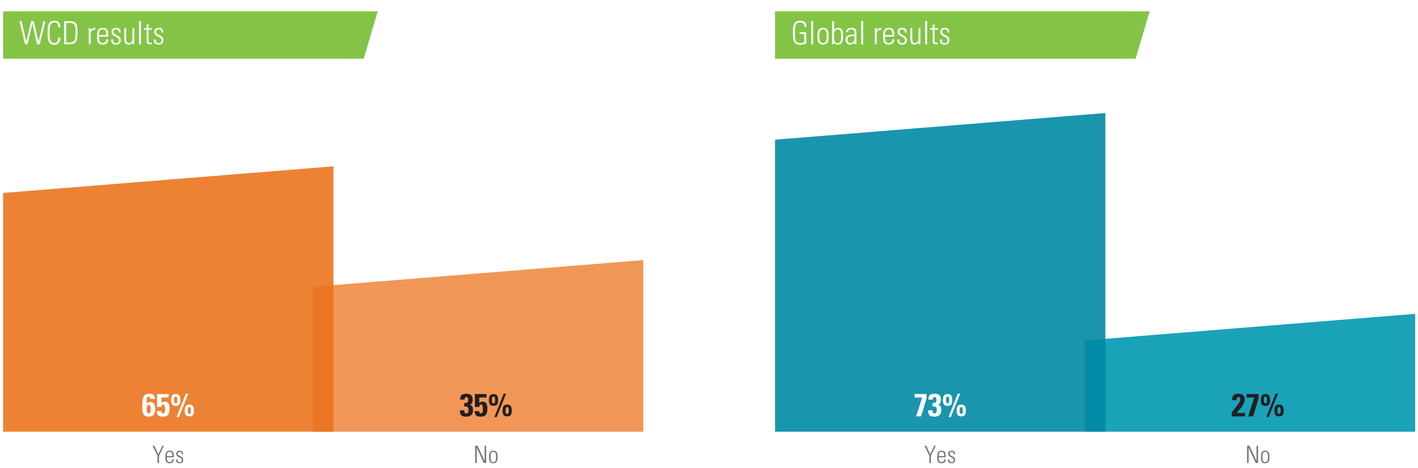


FIGURE 31 **Do you currently invest directly in other businesses?**



Source: WCD Family Business survey

FIGURE 32 Which of these styles best describes you?

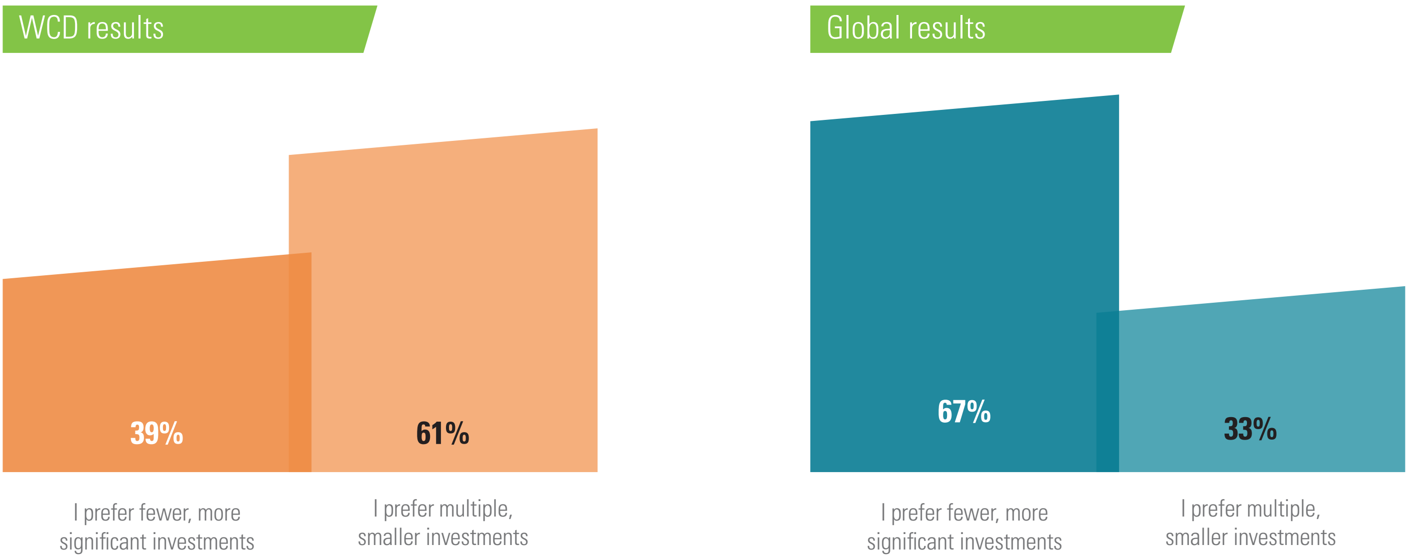
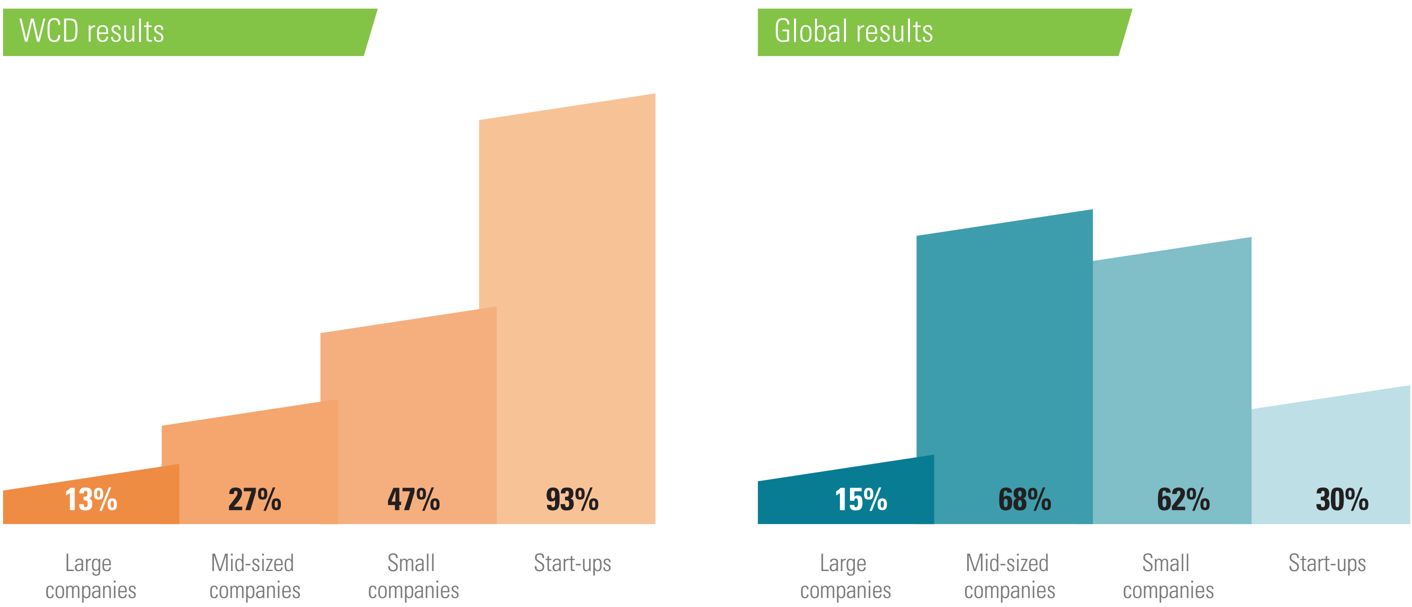


FIGURE 33 What type of companies do you target?
(participants can select multiple options)



Source: WCD Family Business survey

Investment experience with family businesses

Many HNWIs have already invested in family businesses and rate this experience as positive or very positive. The vast majority have invested in one or two family businesses and made it on a personal rather than a more formal basis. Previous positive experiences explain why family businesses stay relatively attractive for HNWIs for future investments.

More than half of the surveyed HNWIs (57 percent) have already invested in a family business in the past (Figure 34) and are generally very happy with their investments, the vast majority (93 percent) rating this experience as positive or very positive in comparison to other types of investments (Figure 35). More than three-fourths of those (79 percent) have invested in one or two family businesses and only one-fifth are serial family business investors, having invested in three or more (Figure 36).

As previously mentioned, HNWIs prefer to control their investment portfolio and self-manage their investment decisions. Over two-thirds (71 percent) of those investing in family businesses do it on a personal basis, rather than a more formal basis, the rest are investing together with a group of individuals, including other HNWIs and family members, and no one has a formal structure with investment managers (Figure 37).

Positive experience of HNWIs with investments in a family business is reflected in their appetite for further investments. Over half of HNWIs surveyed (52 percent) say that they have some interest in investing in family businesses (Figure 38).

FIGURE 34 **Have you previously invested directly in a family business?**

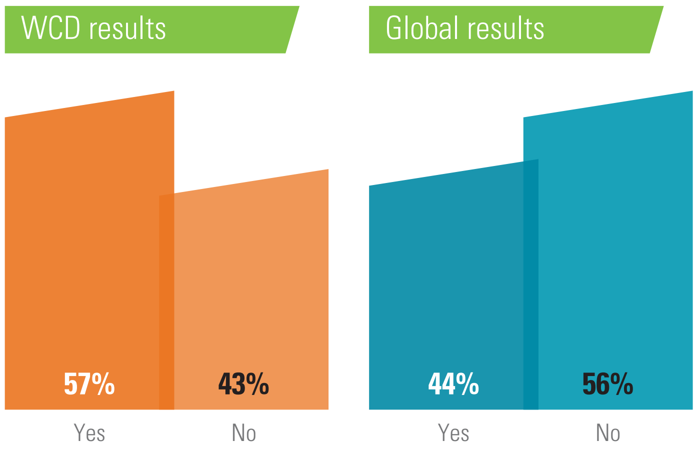
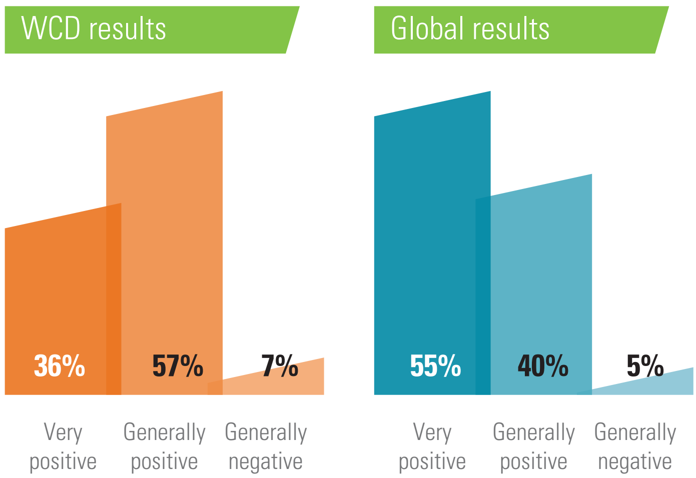


FIGURE 35 **How positive has your experience been of investing directly in family businesses in comparison to your other investments?**



Source: WCD Family Business survey

FIGURE 36 How many family businesses have you invested in?

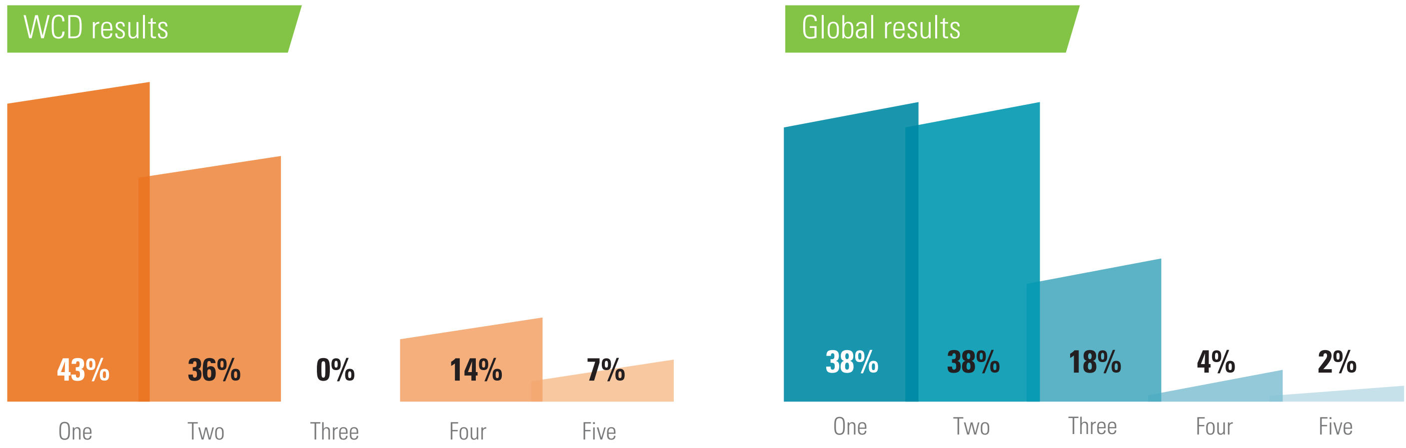
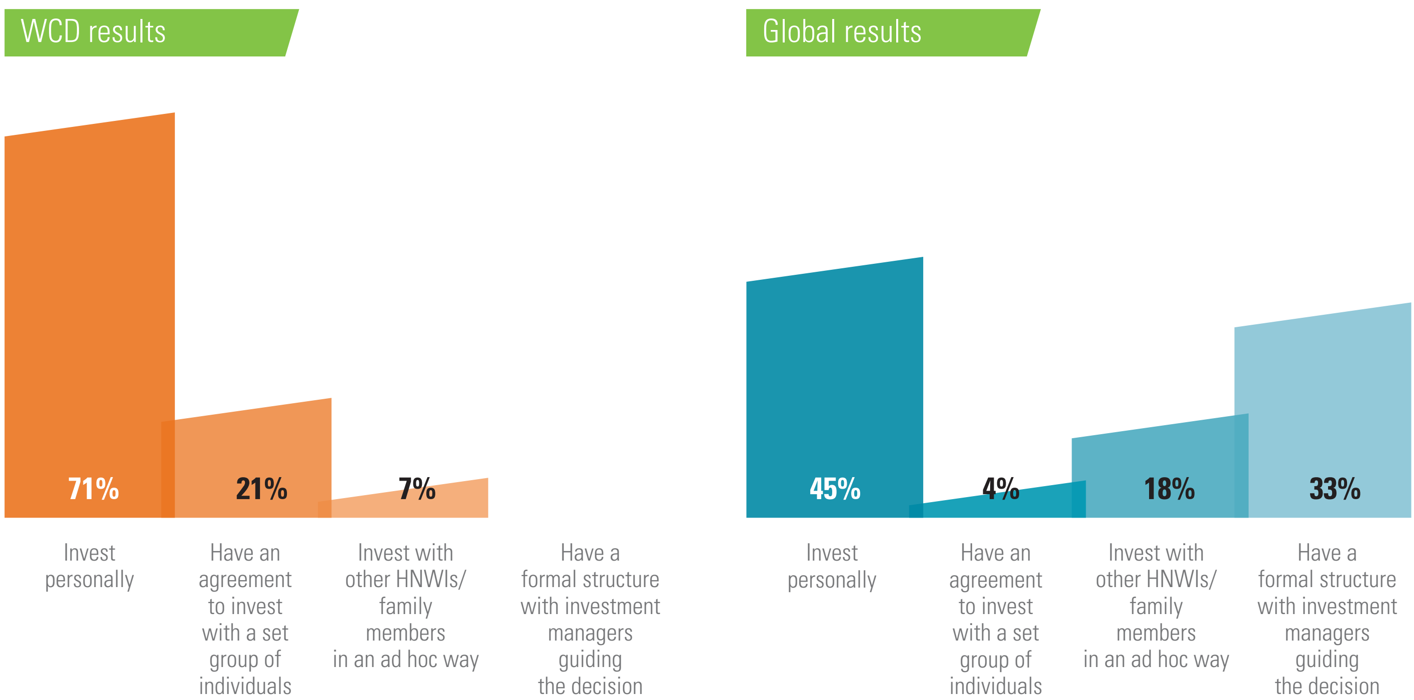
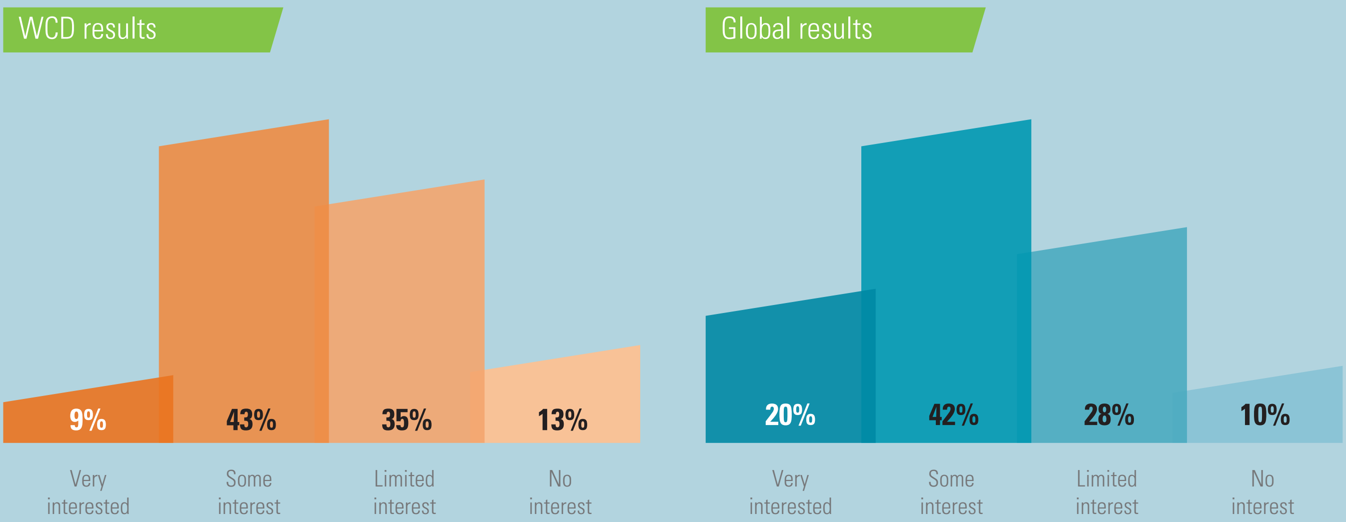


FIGURE 37 What investment modes do you use when investing in family businesses?



Source: WCD Family Business survey

FIGURE 38 To what extent are you interested in investing directly in family businesses?



Source: WCD Family Business survey

KPMG Global Family Business Survey

Similar to the figures from the WCD Survey, many respondents from the Global Survey (44 percent) have already invested in family businesses and rate this experience highly positive. Most of those who have invested targeted one or two family businesses and acted on a personal rather than on a more formal basis. One-third (33 percent), though, used a formal structure with investment managers to guide their decisions.

Investments in family businesses: opportunities

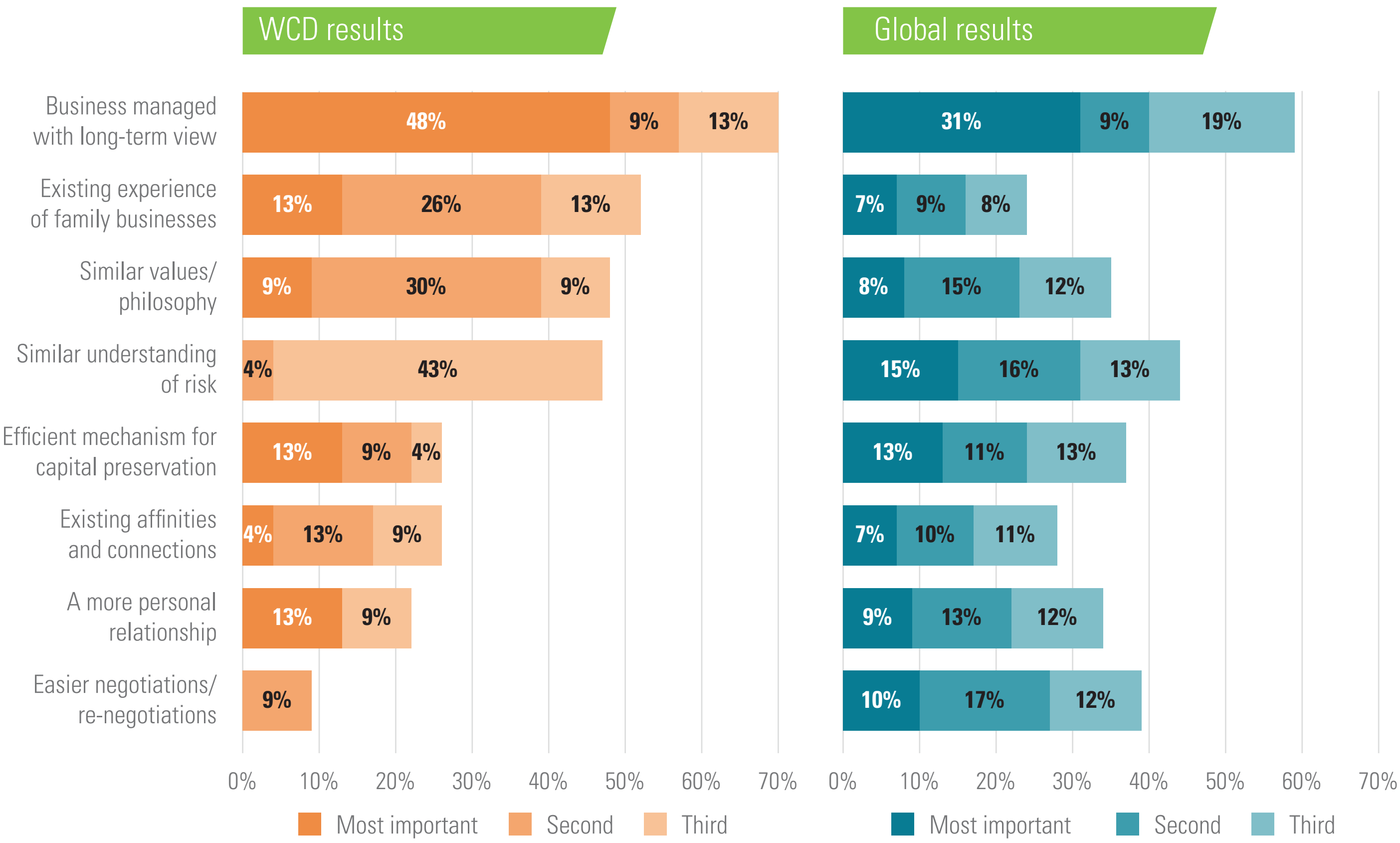
The survey suggests that the expectations and attractions for HNWIs to family businesses match closely with the attributes and characteristics important for family members themselves — a personal approach and shared values, additional knowledge and expertise, a long-term perspective and reasonable risks.

Positive previous experiences reflect a good match between potential partners. The survey results shed a light on what HNWIs are aiming for when investing in family businesses, the advantages they see compared to other types of investments and the pitfalls they strive to avoid.

The main attraction of family businesses to HNWIs is that they are managed with a long-term view, followed by family business experience, a similar understanding of risks and similar values (Figure 39). This matches perfectly to what family businesses were looking for in HNWIs (a similar understanding of risk, the willingness to provide support and advice, shared values, experience of family business and trust), to their appreciation of HNWIs being patient investors. Interestingly, intangible assets are highly important in this type of investment for both investors and investees, due to the 'family' nature of family businesses and the personal, rather than formal, way of managing wealth for HNWIs.

HNWIs are professional and successful managers striving for steady capital growth and moderate risks. Unsurprisingly, the business factors most likely to attract them to family business investments are the business potential for strong organic growth, high profitability and strong cash flows, along with impressive and inspirational management (Figure 40).

FIGURE 39 What factors have/might attract you to investing directly in family businesses?

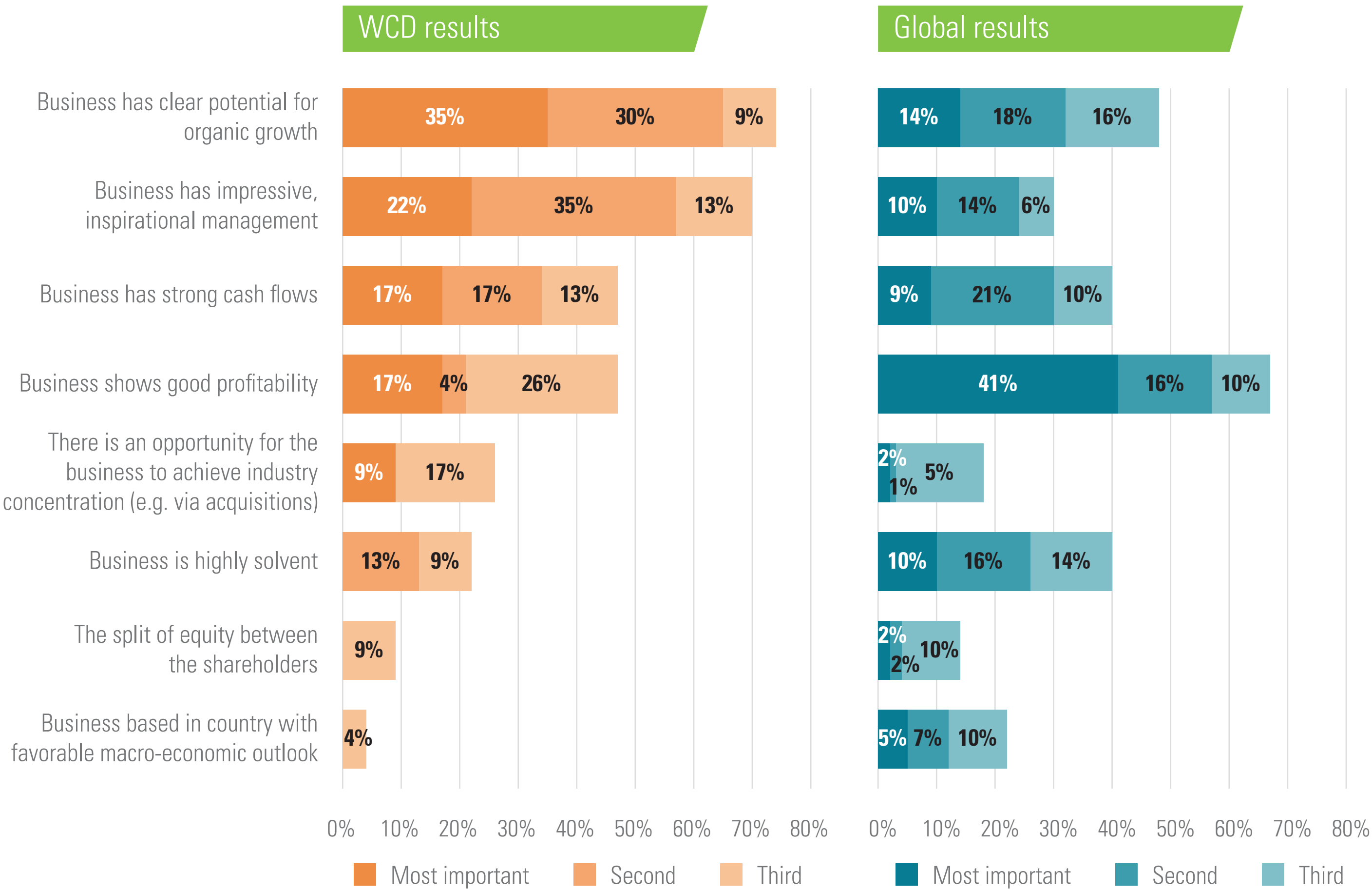


Source: WCD Family Business survey

In terms of governance, the potential to have a board seat and involvement of independent board members are most highly valued, cited by 66 percent and 65 percent of the respondents, respectively (Figure 41). Results suggest it won't be an issue for more than one-third (37 percent) of the surveyed family firms, saying they would be prepared to offer board seats and/or voting rights to external investors (Figure 16). Additionally, those two-thirds of family business respondents who wished to maintain family ownership and control, could be reassured by the very low number of HNWIs (21 percent) mentioning potential to acquire a majority share of the company among important investment goals (Figure 41). This finding differs from the Global Survey where half of the HNWIs were attracted by the potential to acquire a majority stake in the company.

HNWIs' desire to control their investment portfolios is reflected by the fact that the vast majority of respondents (83 percent) would like to regularly express their views to management (Figure 42). It once again fits family businesses who do not want investors to be passive.

FIGURE 40 **If you were to invest in a family business, which of these business factors would be most important?**



Source: WCD Family Business survey

FIGURE 41
If you were to invest in a family business, which of these governance factors would be important to you?

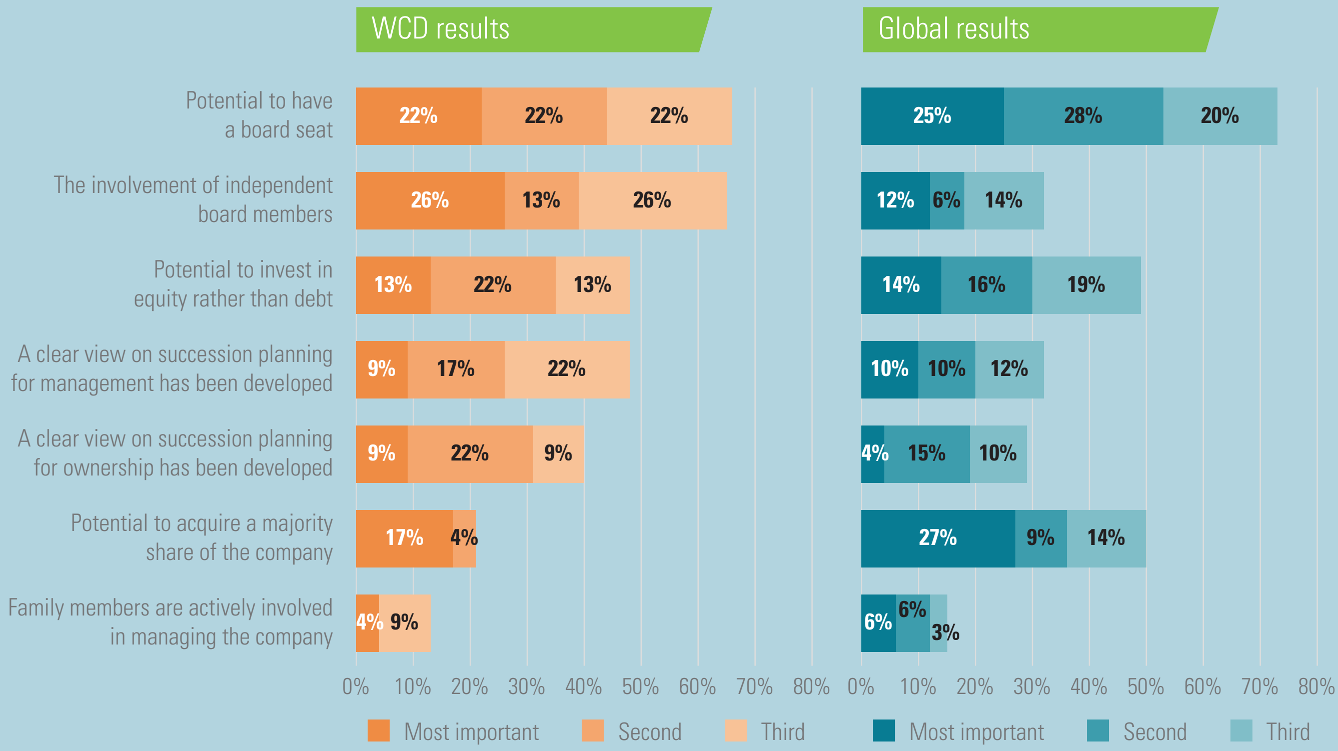
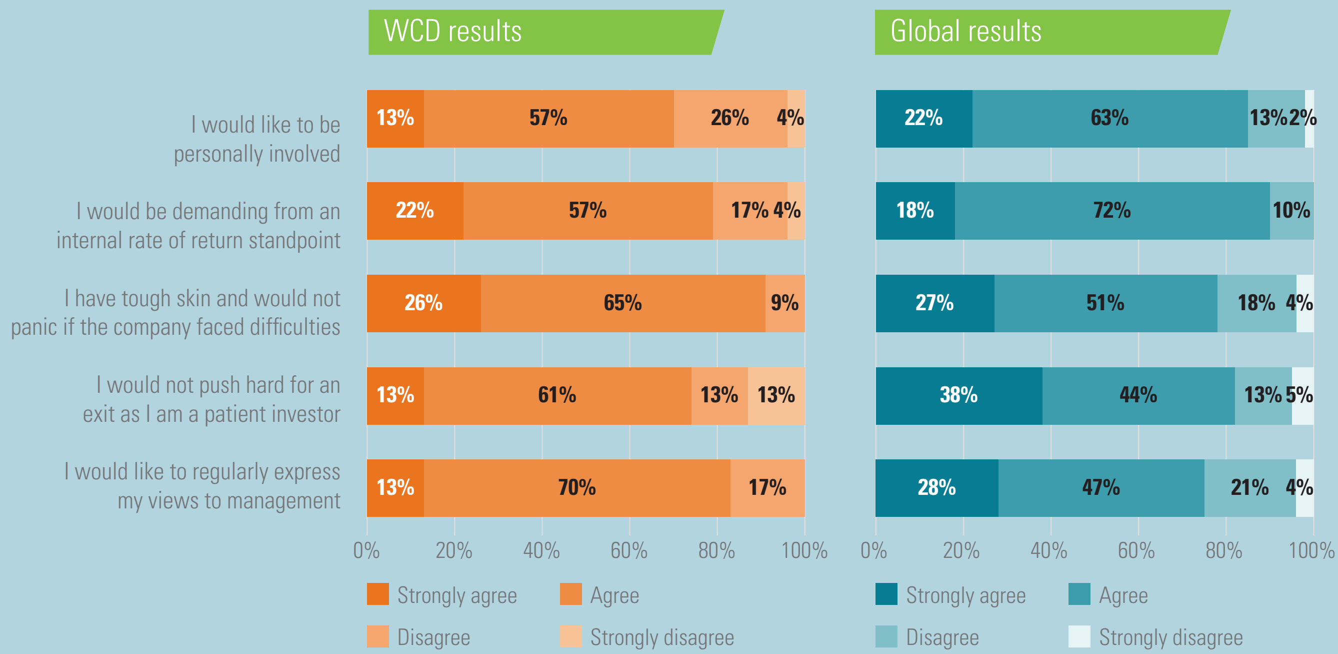


FIGURE 42
For a potential investment in a family business, please indicate the extent to which you agree with these statements



Source: WCD Family Business survey

KPMG Global Family Business Survey

HNWIs from the Global Survey are favorable to family business investments and are mostly attracted by a long-term approach to business management, a similar understanding of risks, as well as efficient mechanisms for capital preservation and easier negotiations — all matching well to what family businesses are looking for.

Likewise the WCD members, in this kind of investment partnership, the HNWIs from the Global Survey rank profitability of the business, potential for growth and strong cash flows, and having a board seat as high. An important difference, though, is that half of them are looking for a majority stake.

Investments in family businesses: pitfalls

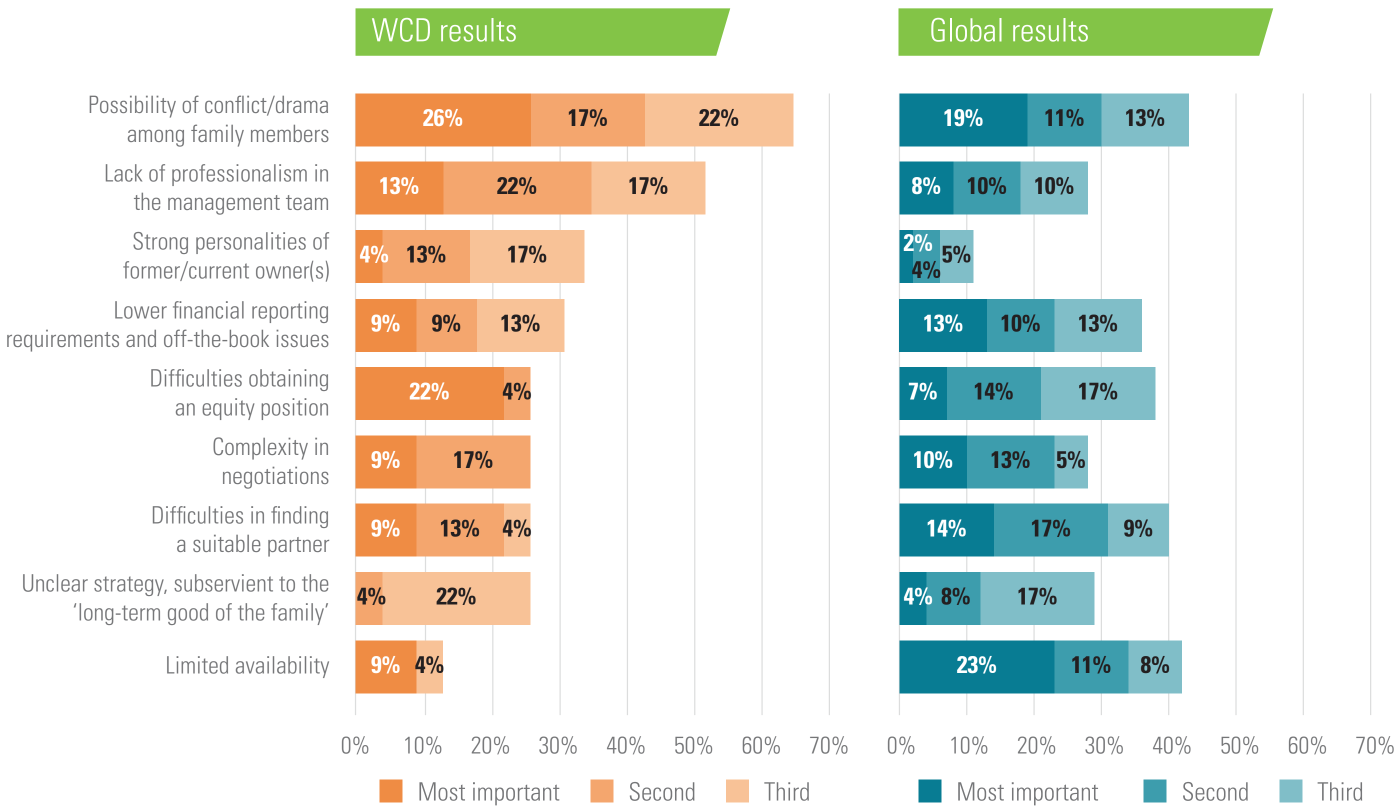
The fears expressed by the family businesses surveyed about the difficulties in finding a suitable partner seem not to be supported by HNWIs. The survey indicates that HNWIs worry about possible conflicts and disagreements within the family and unprofessional management.

As business people and board members themselves, the WCD HNWIs surveyed expect a high level of professionalism from the owners and leaders of family businesses in which they invest. Unsurprisingly, the possibility of conflict and drama among family members and lack of professionalism in the management team were by far the most significant factors to discourage HNWIs from investing in family businesses, cited by over half of HNWIs surveyed, 65 percent and 52 percent, respectively (Figure 43).

Other potential barriers, like complex negotiations, difficulties in obtaining an equity position and difficulties in finding a suitable partner do not seem to be a real issue.

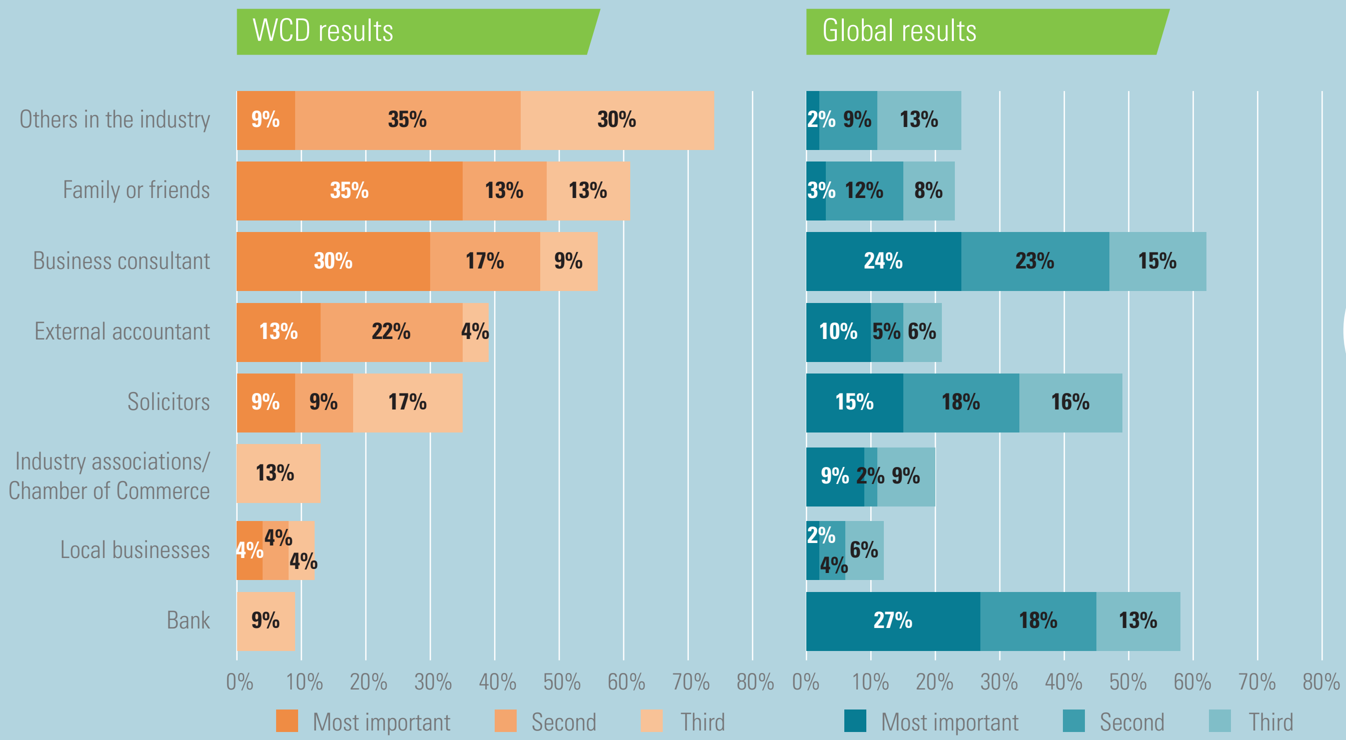
The solution to the challenge of a potential partner search seems evident if you look at those whom HNWIs will approach for advice when investing in family businesses. Others in the industry, family, friends and business consultants top the agenda, being mentioned by more than half of respondents (Figure 44). This presents an opportunity for the advisors to play an integral role in connecting the two groups and provide instructions that could benefit both parties. Additionally, better networking within the family business community could easily facilitate the experience exchange.

FIGURE 43 What factors have/might discourage you from investing directly in family businesses?



Source: WCD Family Business survey

FIGURE 44 **If you were to invest in a family business, who would you approach for advice on how to do this?**



Source: WCD Family Business survey

KPMG Global Family Business Survey

The Global Survey respondents expressed fear about a possibility of conflict among family members, and they are afraid of the limited availability of potential partners, the difficulties in finding them and the difficulties in obtaining an equity position.

Global Survey respondents are more likely to approach business consultants, banks and solicitors for advice, than hope for help from family, friends and business associates.

Conclusion: Key family business findings

1 Retaining majority ownership is important for family businesses.

2 Many family businesses recognize the importance of external influence and the value of independent board members.

3 Like all companies, family businesses need financing. The biggest barrier to financing partnerships is the potential for loss of control and independence.

What distinguishes WCD's family businesses from the global family business community?

WCD Survey respondents

- The business is strongly controlled by the family: two-thirds are fully owned by family members and only one-fifth has a majority of non-family members on the board.
- They are quite ambitious in their plans for acquisitions and development in new geographic markets, even in a short-term perspective.
- They have a greater focus on intangible assets. Trust and shared values are crucial for their choice of investors.

Global Survey respondents

- Though family is important, less than half are fully controlled by family members and around half have more than 50 percent of their governance board composed of non-family members.
- They concentrate on day-to-day operations and new products and services in the short term, postponing more ambitious growth plans for the distant future.
- Long-term orientation, similar understanding of risks and business expertise are the most desired characteristics in external investors.

Key HNWIs findings

1 HNWIs generally self-manage a large proportion of their investments.

2 The majority of HNWIs are looking for investments with reasonable risks and reasonable returns.

3 The main factor that would deter HNWIs from investing in family businesses is the possibility of conflict among investee family members.

What distinguishes WCD's HNWI from HNWIs globally?

WCD Survey respondents

- They are rarely connected to any family business (in the past, present or future), being either self-made millionaires or by inheriting their wealth.
- They mostly invest in start-ups and small businesses.
- While investing in family businesses, they target professionally managed companies with growth potential.

Global Survey respondents

- For the most part, they have some family business experience, either belonging to an established family firm or by building up a family business themselves.
- They chose mid-sized and small companies as their priority investment targets.
- While investing in family businesses, they focus on profitable companies demonstrating potential for growth and strong cash flows.

"A potential fit ... not yet fully uncovered"

Qualitative comments on the survey

In order to bring life to statistics, we interviewed a few WCD members or their representatives (family office). Together, they offer a full array of experiences personally (as HNWIs and as family business members) and through their observation roles on boards or as executives.

The diversity of situations is striking: some of the family businesses are fully private and strongly determined to stay so, others are publicly traded or are considering to go public, and a last category has opened their capital to investors. HNWIs offer similar diversity: some only invest in traded stocks and bonds, others also invest directly in businesses, and the latter have different aspirations regarding their presence on the boards of these businesses. However, a few strong common themes emerge that are very consistent with the survey.

Families like to keep control of the business

This is not a revelation: families are strongly attached to their business, especially when it has gone through a few generations. It is their common project, sometimes part of their identity.

A common thread in the survey is the families' willingness to stay in control. An outside board member expresses it to the extreme: *"They think they can sell and still keep control." Family* businesses have to balance financing, growth pace, dividends and control. The same person observes: *"If there were to be a trade-off, control would come before growth"* and *"They do not have to grow more, contrary to public companies; they would say: 'why would I do that?'"* indicating that family businesses may have different goals from businesses with another type of ownership. Indeed, family business research shows that, for these companies, long-term sustainability comes before short-term profits.

In a fully family-owned business, the family met and took the explicit decision not to open the capital: *"We have agreed as a family that we will stay a family business. It is in our shareholders' agreement. This is not something that we need to re-discuss every year."* For this family business, as for many others, the profitability of the business is sufficient to finance their growth. We also know from family business research that family businesses are very careful to focus their investments and to get a higher return: they manage their own money!

For other family businesses, going public is a way to keep control while opening the capital: a minority of the shares can be quoted, or dual classes can be created, allowing in both cases the family to keep the majority of voting rights. *"We no longer have the fear of loss of control. With an IPO, you are still in control. You do not need to pay a lot to the banks; it is a cheaper way to finance growth."*

Indeed, in countries like France or Germany — and even in the US to a lesser extent — a large proportion of traded firms can be considered family businesses, and they present a successful governance model.

The primary sources of funding are profits and banks

In all cases, consistently with all existing research on family businesses, profits and banks are used to finance the business and keep control.

"We use profits and bank debt. The banks have seen our performance, they want to lend us money."

Sometimes, family members offer additional financial support to the business: *"My brother has other businesses and lends money to the business — some sort of 'bridge financing'. It does not dilute the other owners".*

The issue with outside investors is their exit, and the probability that they have different goals

External investors have a time horizon for their exit and they want to maximize their return: *"Unless you are looking for an exit, I think having an external investor is a hard one. Private equity want out in one to seven years with a return,"* and *"We have not looked at private investors. As entrepreneurs, we never looked at private equity because they would have* *different goals / ways to run the business. They rush you to make a profit because they want to exit at a certain time".*

While HNWIs and family businesses are considered to offer a better potential fit as investors, the question of their time horizon for exit must be addressed.

The cultural 'fit' between the family business and the investor is key — a potential contribution from HNWIs as investors?

Investors need to understand the specificities of family businesses: *"Family businesses are a special thing. You have to have a special mind-set — like for family things — to have sensitivity".*

As an illustration, similar values and appetite for risk/return are very important: *"Similar values are sacred"* tells one of the family business members.

The parties also have to talk about the willingness of the family to keep control, and it is felt that maybe HNWIs are less exit-oriented than classical private equity firms.

One of the cases is a perfect illustration of the need for a cultural, and even emotional, 'fit': *"It was the very first time that they opened the capital. It was a long process. They needed to invest big money to grow. If not, they would have had to sell, so they decided to go with a private equity company. It was a personal thing. The owner of the PE fund is very sensitive to this business sector. They have a common dream, a common vision for the company. There is a strong emotional connection".*

Indeed, HNWIs who invest directly in businesses are doing so for reasons that are not purely financial

Our respondents' asset allocation is 'classical' and focuses primarily on stocks, bonds and real estate. Hedge funds and direct investments in businesses often come next.

When they make direct investments, similarly to the case recounted above, investors seek professional or personal connections with the sector or the business, and want to support the mission of the companies they invest in: *"This is our creative outlet, we do not do it for the financial; there is a meaning, a personal commitment. Some came from people we know". "Now we invest when we feel we understand the business. The odds are better if we know the business."* For another family of investors: *"The experience /skills (of the investors) come into play."*

The commitment of some family members to impact investing or to philanthropy is another illustration of the importance of giving a meaning to investments.

Investment objectives can be quite different within a given HNWI or business family

Our interviewees mentioned very different appetites for risk and entrepreneurship within the same families. Differences can be found between generations or within a sibling group. In both cases, those who are/were closer to business operations (e.g. the family business when there was one) seem more willing to take risks and to be more entrepreneurial. One person observed that men of the family were prone to take more risks — an area for investigation?

Moreover, a HNWI can have different expectations from her investments at different stages in her life.

While the survey indicates that having a board seat is a requirement for a majority of respondents, some HNWIs separate their 'financial' and 'human' investments

While it was clear from our interviews that HNWIs invest in companies where they have some professional and emotional connection, some indicated that they are not looking for a seat on the board. Conversely (and maybe not surprisingly for a WCD member), another HNWI told us that she only invests in conventional assets (stocks and bonds) but offers her *'human capital'* as a board member to businesses and start-ups, thus dissociating financial investments from human contribution.

HNWIs in our interviews, as in the survey, do not particularly target family businesses ... and fear family conflicts

While they target private firms, and often start-ups, they do not expressly focus on family businesses. Consistent with the survey, they fear family conflicts: *"We have good governance in our family business, with external board members. The family values the effort it takes. This is why they would be afraid of family conflicts when investing in another family business. On the other hand, we also have an example of a successful family business … "*

One HNWI fears *"informal arrangements that are to the detriment of investors".*

Several respondents interviewed mentioned the importance of good communication within the family and outlined the positive role that a family council can play as a place for family discussions and decisions.

Building bridges between HNWIs and family businesses

Many elements indicate that the fit could be greater between family businesses and HNWIs (and probably even more so for those from a family business background) than with more financial investors: similar values, longer time horizon and the potential for closer risk/return objectives.

However, several conversations need to take place before such a match, and the 'due diligence' must include tangible and intangible aspects: What are the values and goals of each party? What are the respective appetites for risk and return? Is the investor planning an exit and when? Who would buy their shares then? Do the business owners wish to maintain control or to exit themselves? Would they have the means to buy back the shares of the investor? What will be the level of involvement of the investor on the board and in the operations? Is the family organized to make decisions and address potential conflicts?

But for these conversations to happen, HNWIs and family businesses must find each other: While one of our interviewees expressed a potential interest to invest in family businesses, she wittingly observed that *"It is hard finding them, there is no 'dating service'".*

In fact, the idea of 'families investing in families' has been given airtime for several years,[1] but apart from a few successful examples of such platforms, this concept is still in its early stage. An entrepreneurial opportunity?

We would like to wholeheartedly thank WCD members and the president of a family office recommended by another WCD member, for their time and insights. Thanks to them, we have been able to deepen and expand on our interpretation of the Global Survey and to write the above comments. All the quotes come from the interviews.

Christine Blondel

Interviewed WCD members:

Anne Berner
COB, Valilla Interior, Finland

Carmen Rosa Graham
Member of the Board, Ferreycorp, Interbank, Backus, Entel Perú, Camposol, Peru

Christie Hefner
Former Chairman, CEO, Playboy Enterprises, presently — Chairman, Hatch Beauty, USA

Margaret Pederson
President, Amirexx, LLC, USA

Pacita U. Juan
President/Director, M.D. Juan Enterprises Inc.

Susan Remmer Ryzewic
President and CEO, EHR Investments, Inc., USA

1. See DE VISSCHER F. (2012), "The Plot Does Not Change... Only the Theatre and the Actor!", accessed on www.familybusinesswiki.org.

Methodology

The WCD Survey explored the proposed topics among WCD members located worldwide and representing family businesses and HNWIs. The survey included the combination of quantitative questions and qualitative interviews.

The quantitative responses were received through an online questionnaire from 19 family businesses and 23 HNWIs and are presented graphically.

The qualitative interviews were held with the selected WCD members by Christine Blondel, an Adjunct Professor of Family Business at INSEAD and Senior Advisor to KPMG on Family Business Intelligence, and the analysis and quotes are presented in a separate section *'Qualitative comments on the survey'* at the end of the report.

The comparison with the results of the KPMG Global Family Business Survey *'Family matters: Financing family business growth through individual investors'* (the Global Survey) is cited through the report in separate comment boxes.

You can view the results of the Global Survey and download the full report at: **kpmg.com/familybusinesssurvey** or by contacting:

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